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DEPARTMENT OF CONSUMER AFFAIRS
CALIFORNIA BOARD OF ACCOUNTANCY

FINAL

MINUTES OF THE
February 23, 2006
BOARD MEETING

California Board of Accountancy Office
2000 Evergreen Street, Suite 250
Sacramento, CA 95815
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I. Call to Order.

President Ronald Blanc called the meeting to order at 10:00 a.m. on Thursday, February 23, 2006, at the California Board of Accountancy Office in Sacramento and the meeting adjourned at 12:36 p.m.

Board Members	February 23, 2006
Ronald Blanc, President	10:00 a.m. to 12:36 p.m.
David Swartz, Vice President	10:00 a.m. to 12:36 p.m.
Ruben Davila, Secretary-Treasurer	10:00 a.m. to 12:36 p.m.
Richard Charney	Absent
Donald Driftmier	10:00 a.m. to 12:36 p.m.
Sally Flowers	10:00 a.m. to 12:36 p.m.
Sara Heintz	10:00 a.m. to 12:36 p.m.
Gail Hillebrand	10:00 a.m. to 12:36 p.m.
Thomas Iino	10:00 a.m. to 12:36 p.m.
Clifton Johnson	Absent
Bill MacAloney	10:00 a.m. to 12:36 p.m.
Olga Martinez	10:00 a.m. to 12:36 p.m.
Renata M. Sos	10:00 a.m. to 12:36 p.m.
Stuart Waldman	10:00 a.m. to 12:36 p.m.

Staff and Legal Counsel

Mary Crocker, Assistant Executive Officer
Alice Delvey-Williams, Renewal Continuing Competency Coordinator
Patti Franz, Licensing Manager
Dominic Franzella, Renewal Continuing Competency Analyst
Michael Granen, Deputy Attorney General, Board Liaison
Larry Knapp, Supervising Investigative CPA
Nicholas Ng, Practice Privilege Analyst
George Ritter, Legal Counsel
Theresa Siepert, Executive Analyst
Carol Sigmann, Executive Officer
Aronna Wong, Regulation/Legislation Analyst

Committee Chairs and Members

Roger Bulosan, Chair, Qualifications Committee
Dawn Struck, Member, Administrative Committee

Other Participants

Bruce Allen, California Society of Certified Public Accountants (CalCPA)
Sheri Bango, American Institute of Certified Public Accountants (AICPA)
Melanie Choy, Big 4 Accounting Firms
Julie D'Angelo Fellmeth, Center for Public Interest Law (CPIL)
Conrad Davis, California Society of Certified Public Accountants (CalCPA)
Loretta Doon, California Society of Certified Public Accountants (CalCPA)
Mike Duffey, Ernst & Young LLP
Michelle Elder, Society of California Accountants (SCA)
Kenneth Hansen, KPMG LLP
Ed Howard, Center for Public Interest Law (CPIL)
Rich Jones, Washington Society of CPAs
Art Kroeger, Society of California Accountants (SCA)
Tony Laliberte, Washington Society of CPAs
Cathy Landau-Painter, KPMG LLP
Brianna Lieman, Department of Consumer Affairs (DCA)
David Link, Senator Figueroa's Staff
Richard Robinson, Big 4 Accounting Firms
Hal Schultz, California Society of Certified Public Accountants (CalCPA)
Rick Sweeney, Washington Board of Accountancy
Jeannie Tindel, California Society of Certified Public Accountants (CalCPA)
Rob Troncoso, Center for Public Interest Law (CPIL)
Mike Ueltzen, California Society of Certified Public Accountants (CalCPA)
Ross Warren, Assembly Business & Professions Committee
Hayden Williams, Arizona Society of CPAs

I. Call to Order.

Mr. Blanc called the meeting to order at 10:00 a.m. and welcomed staff, members of the public, and the profession. He indicated that much had been accomplished at the CPC meeting the previous day.

II. Committee on Professional Conduct.

A. Minutes of the January 19, 2006, CPC Meeting.

This agenda item was deferred.

B. Report on the February 22, 2006, CPC Meeting.

1. Consideration and Approval of Statutory Amendments Related to Temporary Practice and/or Implementation of Practice Privilege.

Ms. Hillebrand indicated that her report would cover the discussion from the CPC meeting, the recommended statutory amendments, identification of issues for further action and study, and the CPC's recommended positions on pending legislative proposals. She noted that due to time constraints, the CPC did not get the opportunity to discuss the Frequently Asked Questions (FAQs). Ms. Hillebrand indicated that it was the view of the CPC that Board input into the FAQs can be helpful, however, it is not required. Staff may prepare the material without input from the Board.

Ms. Hillebrand thanked the staff for the extraordinary amount of work that went into preparing for the meetings. She had requested staff to review Mr. Robinson's letter **(Attachment 1)** and provide point by point comments, as to what the law currently requires and where a different result is sought. She noted that this could have involved a different interpretation of the current law, a possible statute change, evaluation of any potential harm to the public, any unintended consequences, and equity between CPAs in California and out-of-state. Ms. Hillebrand noted that as staff began to perform that work, it became clear that there were several overarching policy issues. The CPC meeting was helpful in identifying those matters which could be resolved within a short timeframe. Ms. Hillebrand thanked those who provided public comment at that meeting.

Ms. Hillebrand expressed that the goal of the CPC and the Board was to look at possible temporary statutory changes of the shortest duration related to practice privilege based on the identified and alleged problems while allowing adequate time for a full vetting of the issues. She indicated that she believed it would be a mistake to

propose something now that had not been fully considered with respect to any unintended consequences. Ms. Hillebrand reported that the criteria used for the proposals was whether it would interfere with the protection of the California public, whether it would it create inequities with California CPAs, and whether it would create other unintended consequences. She noted that the CPC and the Board were very aware of the urgency of the matter, especially in relation to the tax season.

Ms. Hillebrand reported that the CPC developed the following proposals for statutory changes.

- Proposed Business and Professions (B&P) Code Section 5050.1 – A statutory amendment that would include a statement that regardless of what statutory authorization is being acted under, if a person or a firm is engaged in any act which is the practice of public accountancy in California for a California client, the Board has jurisdiction over that person or firm.
- Proposed B&P Code Section 5096.12 – A statutory amendment to address the problem experienced by a person who qualifies for and receives a practice privilege but cannot sign on behalf of the firm because the firm is not registered in California. She noted that there are a series of hurdles to registering a firm in California, so the CPC chose not to pursue a firm practice privilege, but instead recommends a waiver of the registration requirement solely for the purpose of the individual holding the practice privilege to be able to sign on behalf of the firm.
- B&P Code Section 5054 – There was significant correspondence from tax practitioners around the country regarding the issue of why the practice privilege was necessary if practitioners are only preparing tax returns and never physically enter California. Ms. Hillebrand indicated that the Board's view has consistently been that this is the practice of public accountancy in California. She reminded the Board that a narrow exception was developed last year for the preparation of tax returns for individuals and for the estates of persons residing in California at the time of death. She indicated that the CPC's recommendations to the Board, with the dissent of the Chair, is that the exception be broadened to tax services. Expanding the exception to tax services would eliminate the problems that have been identified by the profession.

Ms. Hillebrand reported that the CPC recommended the following language as a permanent statutory change as B&P Code Section 5050.1.

"Any person who engages in any act which is the practice of public accountancy in this state consents to the personal, subject matter, and disciplinary jurisdiction of the Board; and is deemed to have appointed the regulatory agency of the state or foreign jurisdiction that issued the person's permit, certificate, license or other authorization to practice as the person's agent on whom notice, subpoenas, or other process may be served in any action or proceeding by or before the Board against or involving that person."

It was moved by Mr. Driftmier, seconded by Ms. Sos, and unanimously carried to adopt the language above as B&P Code Section 5050.1.

Ms. Hillebrand reported that the CPC proposed B&P Code Section 5096.12 to address the issue of a person who qualifies for and receives a practice privilege, but cannot sign on behalf of the firm because the firm is not registered in California.

Ms. D'Angelo Fellmeth indicated that proposed B&P Code Section 5096.12(a)(2) was not self-executing, and she questioned whether it would be implemented through regulation. Ms. Hillebrand noted that the firm would be consenting under B&P Code Section 5050.1 and the concept was that the act of practicing in this state constituted the consent; however, the language would need to be modified. Mr. Granen indicated that the change could parallel the language in proposed B&P Code Section 5050.1. Ms. D'Angelo Fellmeth additionally noted that in proposed B&P Code Section 5096.12(a)(2), the last three words should be changed to "...under this article."

Ms. Sigmann clarified that in order to expedite these changes, nothing can be done by regulation. Any changes must be statutory for urgency purposes.

Mr. Granen recommended the following changes to proposed B&P Code Section 5096.12.

"(a) A CPA firm that is authorized to practice in another state and which does not have an office in this state may engage in the practice of public accountancy in this state through the holder of a practice privilege provided that the practice of public accountancy by the firm is limited to authorized practice by the holder of the practice privilege.
(b) Any firm practicing under this provision consents to the personal, subject matter, and disciplinary jurisdiction of the board with respect to any practice under this chapter.

(c) The board may revoke, suspend, or otherwise restrict or discipline the firm for any act which would be ground for discipline against a holder of a practice privilege through which the firm practices."

It was moved by Ms. Sos, seconded by Ms. Flowers, and unanimously carried to adopt the proposed B&P Code Section 5096.12 with the changes identified above.

Ms. Hillebrand reported that it was the view of the CPC that these temporary statutory revisions have the shortest sunset timeframe possible while still allowing a full vetting of the issues. She requested staff to identify the time necessary for the Board to complete the entire review process. Ms. Hillebrand noted that this would be a substantial process, and the focus of the Board for the next two years, and would therefore require extending the current peer review date.

Ms. Sigmann reported that she was recommending January 1, 2011, as the sunset date for the temporary provisions being proposed. Between March and early summer of this year she would anticipate implementing the changes in the legislation currently being developed. Meetings during 2007 would address procedural changes, and if all goes well, the changes could be enacted in 2008. That would provide a year to notify all interested parties of the impending changes. Ms. Sigmann noted that the Board was up for Sunset Review in 2009 and it would be providing a progress report to the Legislature related to this issue. Ms. Hillebrand indicated that although the CPC did not have this date to consider yesterday, she was satisfied that it was ambitious but reasonable.

Mr. Robinson requested that the provision for the exception on tax services move forward without a sunset date. If that was not possible, he believed that the sunset date should be the same as the practice privilege sunset date, January 1, 2011, for consistency purposes.

Mr. Swartz questioned the benefits of having a sunset date of January 1, 2010, versus the practice privilege sunset date of January 1, 2011. Ms. Hillebrand believed that the earlier date provided a clear statement that these are not ultimate solutions, however, it is a temporary fix designed to create a window of opportunity for the Board to consider all of these issues.

Mr. Robinson restated that he was requesting that the sunset date be January 1, 2011, so that practitioners can be aware of the requirements prior to beginning a new tax season. He indicated that

if there are different sunset dates, it may require the profession to pursue a different bill, and he would prefer not to do that.

Ms. Hillebrand indicated that she wanted to send a message that the Board would accomplish the work in the shortest amount of time possible.

It was moved by Ms. Sos, seconded by Mr. Swartz, and carried for the sunset date for B&P Code Sections 5050(b), 5054, and 5096.12 to be January 1, 2011. Ms. Hillebrand was opposed.

Ms. Hillebrand indicated that there had been significant correspondence from tax practitioners around the country regarding the issue of practice privilege. She reported that the CPC was recommending to the Board, with the dissent of the Chair, that the exception in B&P Code Section 5054 be broadened to include tax services on a temporary basis. It was noted that expanding the exception to include tax services would eliminate many of the problems that have been identified by the profession.

Ms. Hillebrand indicated that she was not sufficiently informed at this stage to be comfortable that there would be no harm to the California public from the expansion from tax returns to tax services, and for that reason she was in dissent. She additionally expressed her concern that expanding beyond tax returns was substantial and would create gray areas about things that you no longer need a licensed individual or firm to do. Ms. Sos indicated that she favored this amendment because in the extensive discussion yesterday, she was persuaded that the phrase "tax services" is well understood by the profession and also heavily regulated by the Internal Revenue Service (IRS) and the Franchise Tax Board (FTB).

Mr. Robinson indicated that all of his firms are registered in California; however, tax practitioners outside of California want to be able to sign a tax return under this exemption. The language with the use of the term "firm" in B&P Code Section 5054 may deprive practitioners who do not physically enter California who work for a firm that is registered in California from using this exception. Mr. Duffey believed that a clause was necessary to clarify that the exception would apply to either an individual or a person in a California registered firm, thereby, treating out-of-state practitioners, registered and unregistered firms the same.

Ms. Wong indicated that she believed that Mr. Robinson's concern was addressed through the temporary and incidental practice provision proposed for B&P Code Section 5050(b). Mr. Robinson

indicated he believed that B&P Code Section 5054 should include the clarification as well.

Mr. Iino indicated that B&P Code Section 5054 only applied to the profession and there is more than enough guidance to what tax services represents.

Ms. Hillebrand reported that the CPC recommended the following language for B&P Code Section 5054.

"(a) Notwithstanding any other provision of this chapter, an individual or firm holding a valid and current license, certificate, or permit to practice public accountancy from another state may provide tax services without obtaining a permit to practice public accountancy issued by the board under this chapter or a practice privilege pursuant to Article 5.1 (commencing with Section 5096) provided that the individual or firm does not physically enter California to practice public accountancy pursuant to Section 5051, does not solicit California clients, and does not assert or imply that the individual or firm is licensed or registered to practice public accountancy in California.
(b) The board may, by regulation, limit the number of tax returns that may be prepared pursuant to subdivision (a).
(c) This section shall become inoperative on January 1, 2011, and as of that date is repealed."

It was moved by Mr. Driftmier, seconded by Mr. Iino, and carried to approve the above language for B&P Code Section 5054. Ms. Hillebrand was opposed.

Ms. Hillebrand reported that the CPC had an extensive discussion regarding temporary and incidental practice. She noted that the restrictions approved by the Board at its last meeting related to the foreign accountants provided an excellent model for similar restrictions on temporary and incidental practice by out-of-state CPAs. The restrictions included not holding out as a California CPA, not soliciting of clients in California, and submitting to the jurisdiction of the Board.

Ms. Sos explained why the Board still needed some form of temporary and incidental practice. The tax services issue was resolved by B&P Code Section 5054, and the triggering of firm registration was resolved by B&P Code Section 5096.12. However, staff could still receive questions regarding what exactly is the practice of public accountancy in California, whether it included litigation support, consulting, and expert witness testimony. Ms. Sos

indicated that in order to resolve the additional inadvertent barriers created by practice privilege, the CPC wanted to recreate a limited version of temporary and incidental practice on a temporary basis to provide the Board with the time and the opportunity to address the serious and difficult issues related to the definition of the practice of public accountancy in California before adopting a permanent solution.

Ms. Hillebrand indicated that the Board was in a difficult position because one of the benefits of practice privilege as described by those who advocated for it meant the elimination of temporary and incidental practice allowing the Board to know who was in California practicing.

Ms. Sos believed that it was imperative to communicate to everyone that the limited and very clearly defined restoration of temporary and incidental practice was temporary and solely for the purpose of giving the Board time to resolve some very serious issues in the application of Practice Privilege.

Ms. Hillebrand reported that the CPC recommended that the Board approve the following language for B&P Code Section 5050.

"(a) Except as provided in subdivisions (b) and (c) of this section, subdivision (a) of Section 5054, and Section 5096.12, no person shall engage in the practice of public accountancy in this state unless the person is the holder of a valid permit to practice public accountancy issued by the board or a holder of a practice privilege pursuant to Article 5.1 (commencing with Section 5096).
(b) Nothing in this chapter shall prohibit a certified public accountant, a public accountant, or public accounting firm lawfully practicing in another state from temporarily practicing in this state incident to practice in another state provided that the individual or firm does not solicit California clients and does not assert or imply that the individual or firm is licensed or registered to practice public accountancy in California. This subdivision shall become inoperative on January 1, 2011, and as of that date is repealed.
(c) Nothing in this chapter shall prohibit a person who holds a valid and current license, registration, certificate, permit or other authority to practice public accountancy from a foreign country, and lawfully practicing therein, from temporarily engaging in the practice of public accountancy in this state incident to an engagement in that country provided that:
(1) The temporary practice is regulated by the foreign country and is performed under accounting or auditing standards of that country.
(2) The person does not hold himself or herself out as being the

holder of a valid California permit to practice public accountancy or the holder of a practice privilege pursuant to Article 5.1 (commencing with Section 5096)."

Note: The language in subdivision (c) was previously approved by the Board, recommended to the Legislature, and is currently contained in SB 503.

It was moved by Ms. Hillebrand, seconded by Mr. Driftmier, and unanimously carried to approve the proposed changes to Business and Professions Code Section 5050.

Ms. Hillebrand reported that the CPC discussed and was recommending proposed changes to B&P Code Section 5088 that would not require an individual who is the holder of a current and valid license from any state to obtain a practice privilege during the time that he or she has a pending application for licensure in California. She noted that prior to practice privilege, these applicants were permitted to practice while their applications for licensure were pending and that staff had tracked them through a manual system.

Ms. Hillebrand added that since practice privilege has been implemented, the manual tracking system had been abolished and these applicants must obtain a practice privilege while pending licensure in California. She indicated that the CPC had developed the proposed changes with incomplete information. Further discussion with staff identified that this would impact a small number of applicants and the manual tracking system had been eliminated. Ms. Hillebrand indicated that based on this additional information, it was her opinion as CPC Chair that this recommendation was no longer a viable option. She did note that the CPC had not yet considered this additional information.

Ms. Franz added that the staff originally responsible for the manual tracking system have since been redirected and are focused on processing applications for individual and firm licensure. She indicated that the Board had received no negative comments from applicants regarding this change and that it does not seem an appropriate use of staff resources to reimplement the manual system versus processing applications more quickly. Based on this information, the Board concurred that no change should be made to the current B&P Code Section 5088.

Ms. Hillebrand indicated that the language proposed for B&P Code Section 5054.1 is complimentary language to the consent to jurisdiction language in proposed B&P Code Section 5050.1. She noted that it is the procedural piece on how the Board would assert its jurisdiction.

Ms. Hillebrand reported that the CPC recommends that the Board approve the following language for B&P Code Section 5054.1.

"The board may revoke, suspend or otherwise restrict or discipline the authorization to practice under subdivisions (b) or (c) of Section 5050, or subdivision (a) of Section 5054, or Section 5096.12 for any act which would be a violation of this chapter or ground for discipline against a licensee or practice privilege holder, or ground for denial of a license or practice privilege under the Code. The provisions of the Administrative Procedure Act, including, but not limited to, the commencement of a disciplinary proceeding by the filing of an accusation by the board shall apply to this Section. Any person whose authorization to practice under subdivisions (b) or (c) of Section 5050, or subdivision (a) of Section 5054, or Section 5096.12 has been revoked may apply for reinstatement of the authorization to practice under subdivisions (b) or (c) of Section 5050, or subdivision (a) of Section 5054, or Section 5096.12 not less than one year after the effective date of the board's decision revoking the temporary practice authorization unless a longer time, not to exceed three years, is specified in the board's decision revoking the temporary practice authorization."

It was moved by Mr. Driftmier, seconded by Ms. Sos, and unanimously carried to approve the above language for B&P Code Section 5054.1.

Ms. Hillebrand reported that due to the urgency of the work related to Practice Privilege, the peer review report date would also need to be delayed to January 1, 2011.

Ms. Hillebrand identified the following issues that would require further study:

- Out-of-state licensees seeking to qualify as an individual for practice privilege through NASBA – costs and delay issues.
- Substantial equivalency.
- Evaluation of requiring 150 hours of education when applicants can get licensed in California with 120 hours.
- Defining what constitutes the practice of public accountancy in California.

- Whether additional exemptions should be added to B&P Code Section 5054.
- Continued study of the temporary exemption adopted regarding tax services.
- Whether any of the temporary statutory changes should become permanent.
- The balancing of public protection and knowing who is practicing in this state through practice privilege, while not creating barriers to entry for licensed out-of-state practitioners.
- Interplay between firm registration and the individual holding a practice privilege.

Ms. Hillebrand wanted the ability to amend the minutes to include any issues for further study that she failed to mention previously.

Ms. D'Angelo Fellmeth requested to reopen the discussion regarding the necessity of reinstating temporary and incidental practice. She indicated that the expansion of the exception in B&P Code Section 5054 to include all tax services resolved the tax problem. The creation of B&P Code Section 5096.12 resolved the firm registration problem by allowing individuals with a practice privilege to sign on behalf of the firm even if it is not registered in California.
Ms. D'Angelo Fellmeth indicated that she believed that, with those proposed statutory changes, reinstating temporary and incidental practice was not required. In addition, she believed that the temporary five-year period was excessively long.

Ms. Sos indicated that there were practitioners from seven or eight states that are not substantially equivalent and those individuals cannot qualify for a practice privilege. Those are the individuals who need the limited version of temporary and incidental practice.
Ms. D'Angelo Fellmeth noted that if the Board reconsidered the issue of allowing anyone with a valid license from another state to qualify for a practice privilege, it would address that group of individuals and it would not need to restore temporary and incidental practice.

Ms. Sos added that the other benefit of reinstating the limited version of temporary and incidental practice is that it would address the gray areas. It will also allow the Board time to deliberate the issue of what activities constitute the practice of public accountancy in California as well as whether there should be additional exceptions identified in B&P Code Section 5054 such as expert witness testimony, litigation support, or consulting services.

Ms. D'Angelo Fellmeth indicated that the issue of whether the nature, quality, and location of services being provided would trigger the

necessity of obtaining a California license is not a new issue. The profession has always had to consider that. She noted that prior to January 1, 2006, individuals and firms engaged in work that brought them in contact with the state of California had to determine whether that work was temporary and incidental or whether it required licensure. Ms. D'Angelo Fellmeth noted that the new answer was practice privilege. She urged the Board not to reopen this gaping offensive loophole that had been closed.

Ms. Hillebrand indicated that she believed that this is a very close question. She noted that she did not believe that waiving substantial equivalency was a viable solution.

Mr. Robinson reported that there were many areas in question that would need to be defined as exceptions to the practice of public accountancy. He appreciated the work of the Board in resolving these issues and urged the Board to maintain its earlier position.

Mr. Blanc reiterated that what the Board has brought back in with temporary and incidental practice are important restrictions, notifications and expansion of the Board's jurisdiction. Mr. Blanc noted that it was a very difficult decision for Ms. Hillebrand, Ms. Sos, and himself, although, he was somewhat comforted by the restrictive provisions that had been added.

Ms. Sigmann reported that it was very difficult for staff to be in this position of not being able to answer questions regarding practice privilege. She indicated that the Board has a broad definition of the practice of public accountancy in B&P Code Section 5051 and staff have been struggling with its application to practice privilege ever since implementation. Ms. Sigmann reported that the reason staff supported this proposed change is that it is necessary until there is further clarity to B&P Code Section 5051 as it relates to practice privilege.

Ms. D'Angelo Fellmeth commented that Board members are not sitting at this table as practitioners. The role of a Board member is to protect the public interest. She indicated that it is the primary priority of Board members to protect the public and she believed that practice privilege provided much more consumer protection than temporary and incidental practice. Ms. D'Angelo Fellmeth believed that the practice privilege program with the other changes discussed could move forward without reinstating temporary and incidental practice. Ms. D'Angelo Fellmeth urged the Board to consider her thoughts.

There was no action taken by the Board to reconsider its previous decision regarding the implementation of limited temporary and incidental practice. The Board would be studying this issue over the next several months.

Ms. Hillebrand indicated that the revised language to Section 5054 had just been distributed to address the concern communicated by Mr. Robinson. This language reads:

"(a) Notwithstanding any other provision of this chapter, an individual or firm holding a valid and current license, certificate, or permit to practice public accountancy from another state may provide tax services without obtaining a permit to practice public accountancy issued by the board under this chapter or a practice privilege pursuant to Article 5.1 (commencing with Section 5096) subject to the restrictions that the individual or firm does not physically enter California to practice public accountancy pursuant to Section 5051, does not solicit California clients, and does not assert or imply that the individual or firm is licensed or registered to practice public accountancy in California.
(b) Notwithstanding subdivision (a), any firm which is licensed to practice public accountancy in this state may provide the services set forth in subdivision (a) through individuals qualified to practice under subdivision (a) however the restrictions of subdivision (a) shall not apply to the firm.
(c) The board may, by regulation, limit the number of tax returns that may be prepared pursuant to subdivision (a).
(d) This section shall become inoperative on January 1, 2011, and as of that date is repealed."

Mr. Granen indicated that the purpose of these changes was to remove the unintended restrictions current B&P Code Section 5054 places on CPAs employed by registered firms and put them on equal footing with CPAs employed by unregistered firms. Mr. Robinson indicated that he strongly supported the changes.

It was moved by Ms. Sos, seconded by Ms. Flowers, and unanimously carried to approve the revised language to Business and Professions Code Section 5054.

Ms. Hillebrand indicated that several Board members and members of the public have communicated concern to Mr. Blanc as to how the Board actions would be communicated during the Legislative process. She noted that staff have every intent to communicate as clearly and as completely as possible; however, staff do not have the discretion to waive or make any statements of non-enforcement of

current provisions of law. Ms. Hillebrand indicated that the Board will work as quickly and effectively as possible on the proposed statutory changes.

Mr. Blanc reported that there would be communication with all interested parties that the Board had taken positive action in response to requests and staff will be preparing material for distribution.

Mr. Robinson indicated that there was a provision in the Constitution that you cannot retroactively legislate. He suggested communicating to the public using legislative intent language that could be drafted to express that the practice privilege legislation enacted last year had unintended consequences and this current piece of pending legislation is meant to correct those. Mr. Robinson noted that if Senator Figueroa agreed with that language, it could then be posted on the Board's Web site in lieu of the current FAQs.

Mr. Blanc indicated that he wanted a communication to go directly to the profession.

Ms. Bango, AICPA representative, committed to working with CalCPA and the Board to communicate to the AICPA's 340,000 members the positive action taken by the Board, and she indicated that the AICPA has several mechanisms to accomplish that. Ms. Bango indicated that because of California's practice privilege issue and other concerns that have been raised across the country, the AICPA had established a toll-free number and a dedicated e-mail with staff exclusively to answer questions related to these issues. She assured the Board that she would work with staff and CalCPA to ensure that everyone is comfortable with the language that the AICPA would be communicating nationwide.

Mr. Allen indicated that CalCPA would communicate the actions taken by the Board to its members as well as the Executive Directors of other state boards. He indicated that he would coordinate the message so that it is uniform as not to raise further confusion. Mr. Allen added that it had been a productive meeting and he believed that the Board was headed in the right direction to clarify the issues.

Ms. Hillebrand indicated that she would be happy to work with the Board President and the Executive Officer to develop the legislative intent language. She also believed that the language should include the reason why the changes are being proposed as temporary, that they were developed in response to the pending tax season, and that

there will be a further study of all of the issues. Mr. Blanc requested that Ms. Hillebrand work with Ms. Sos and Ms. Sigmann to draft the legislative intent language.

In response to the request to remove the FAQs from the Board's Web site, Ms. Hillebrand indicated that she believed that decision was within the discretion of the Executive Officer. She added that she had reviewed one of the letters that staff had received and she hoped that it was not representative of the profession. It was a highly unprofessional attack on staff that no one should have to experience in the course and scope of their employment.

2. Consideration of Legislation Related to Temporary Practice and/or Implementation of Practice Privilege.

   a. Report and Recommended Position on SB 503, Figueroa.

      Ms. Hillebrand reported that SB 503 contained the following statutory changes that had been previously approved by the Board: 1) the fee change language, 2) the peer review language which needed to be modified with the date as January 1, 2011, and 3) the foreign accountant exception language.
      Ms. Hillebrand noted that legislative counsel recommended removing the word "primarily" from the language approved by the Board at its January 20, 2006, meeting. Ms. Hillebrand indicated that the CPC determined that even with the changes that the Board adopted today, it was necessary to move forward with the foreign accountant language.

      Ms. Hillebrand reported that the CPC recommended that the Board adopt a SUPPORT position on SB 503.

      Mr. Robinson requested that SB 503 be amended to include all of the language that had been approved at this meeting.
      Ms. Hillebrand indicated that the CPC did discuss that idea and had no policy objections to it; however, it was the view of the committee that the strategic decision on how to present this information to the Senator and other members of the Legislature was within the Executive Officer's discretion. Mr. Robinson indicated that he supported the work product and wanted to move it expeditiously, and that his colleague, Mr. Allen, would not support SB 503 unless the language that was adopted by the Board today is amended into that bill. Ms. Sigmann indicated that it was her intention to include the language in SB 503.

Mr. Allen indicated that on behalf of CalCPA, it had no issue with anything currently in SB 503, but its position is that the bill is incomplete. He reported that with the proposed changes adopted today amended into the bill, CalCPA would support it.

It was moved by Ms. Hillebrand, seconded by Ms. Sos, and unanimously carried to adopt a SUPPORT position on the current language in SB 503.

b. Report and Recommendation Position on AB 1868, Bermudez, Accountancy: Licensure.

Ms. Hillebrand reported that the Board had been provided with draft amendments to AB 1868, dated February 13, 2006. **(See Attachment 2.)** She noted that this bill was currently a "work in progress," however, the Board needed to look at the text currently available. Ms. Hillebrand indicated that there was a report from Deputy Attorney General Granen that suggested this language would create serious issues regarding the Board's jurisdictional ability, particularly in its ability to prohibit unlicensed practice. The amendments would also broaden B&P Code Section 5054 beyond the proposed amendments adopted by the Board today. Also, it proposed a later sunset date than what the Board adopted.

Ms. Hillebrand reported that for those reasons, the CPC was recommending that the Board adopt an OPPOSE UNLESS AMENDED position on AB 1868. She indicated that if the bill begins to move forward, staff could then communicate the Board's position to the Legislature. She added that she was hopeful that it would not be necessary for the Board to use this position.

It was moved by Ms. Hillebrand, seconded by Mr. Swartz, and carried to adopt a position of OPPOSE UNLESS AMENDED on AB 1868. Ms. Sos was opposed.

Mr. Allen indicated that it was CalCPA's intention to request that the author hold this bill and not move it forward in its current form. He noted that as SB 503 makes progress, this bill could become a vehicle to assist in moving SB 503 forward.

Mr. Robinson indicated that the fee issue might be controversial to the Republicans in the Legislature. If that happens, Mr. Allen had agreed to put the Board's fee provisions in a bill that the profession would support.

DISCUSSION OF SIGNIFICANT ISSUES RELATED TO TEMPORARY PRACTICE AND/OR THE IMPLEMENTATION OF PRACTICE PRIVILEGE

INTRODUCTION

This paper provides background information for consideration of significant issues related to temporary practice and/or the implementation of the Practice Privilege Program. Issues related to substantial equivalency requirements, firm registration requirements, and the question of "What constitutes a California client?" are discussed (CPC Agenda Items III A, B, and C). For each of these issues, there is a description of the issue, information regarding relevant provisions of the Accountancy Act, background and history information, and a discussion focusing on key concerns. The background and history portion of the section titled "Substantial Equivalency Requirements" provides an overview of how the concept of "substantial equivalency" has been addressed in California as well as providing a historical perspective on the overall development of the practice privilege statutes. The conclusion (beginning on page 10) relates to all of the issues discussed in this paper.

A. SUBSTANTIAL EQUIVALENCY REQUIREMENTS

ISSUE:

The practice privilege statutes permit out-of-state CPAs meeting specified qualifications to practice in California under a practice privilege without obtaining a California license. The qualifications for practice privilege were based on the Uniform Accountancy Act's (UAA's) concept of "substantial equivalency." Recently, concerns have been raised that these "substantial equivalency" requirements obstruct rather than facilitate the cross-border movement of qualified practitioners.

RELEVANT PROVISIONS OF THE ACCOUNTANCY ACT:

The practice privilege provisions are located in Sections 5096 – 5096.11 of the Business and Professions Code. In addition, Business and Professions Code Section 5093 contains California's licensure requirements that are deemed to be substantially equivalent by the National Association of State Boards of Accountancy (NASBA). (See Attachment 1 for the text of these laws.)

Under the basic requirements for practice privilege contained in Section 5096 a licensee of another state has three options to qualify for practice privilege: (1) to have continually practiced public accountancy as a CPA under a valid license for at least four of the last ten years; (2) to hold a license from a state which has been determined by the Board to have education, examination, and experience qualifications for licensure substantially equivalent to California's qualifications under Section 5093, i.e. to be

licensed in a "substantially equivalent state"; or (3) to possess education, examination, and experience qualifications for licensure which have been determined by the Board to be substantially equivalent to California's requirements under Section 5093. Other provisions of the practice privilege statutes include a fee requirement, a list of potentially disqualifying conditions, and provisions for the administrative suspension and discipline of the practice privilege.

For consistency, Section 5088 of the Business and Professions Code was amended to eliminate the interim practice provision under which an out-of-state licensee had practice rights while the application for licensure was pending. In its place this individual was required to obtain a practice privilege (see Attachment 1).

BACKGROUND AND HISTORY:

As part of its 2000 Sunset Review, the Board began evaluating its statutes and regulations for conformity with the UAA, a model accountancy act developed jointly by NASBA and the American Institute of Certified Public Accountants (AICPA).

The edition of the UAA (UAA, third edition) considered by the Board emphasized the concept of "substantial equivalency" which included two components. One component of substantial equivalency involved the establishment of uniform licensure requirements nationwide. This included the requirement that, to become licensed, applicants must have met the "150 Hour Requirement" (150 semester units of education), pass the Uniform CPA Examination, and complete a minimum of one year of experience. States with accountancy acts that included these licensure requirements were deemed to be substantially equivalent. The second component of substantial equivalency focused on the free movement of CPAs across borders. Under the UAA model, CPAs meeting substantial equivalency requirements either by being licensed in a substantially equivalent state or by individually meeting the requisite education, exam, and experience requirements would be able to engage in cross-border practice after notifying the other state board of their presence. The UAA did not include a temporary practice provision.

In its 2000 Sunset Review Report, the Board proposed the 150-Hour Requirement and other law changes so that California could be deemed a substantially equivalent state. This proposal proved to be controversial. As a compromise, the two licensure options currently in California law were enacted – Business and Professions Code Sections 5092 and 5093. Section 5092 conforms closely to the Board's previous licensing requirements. In addition to passage of the Uniform CPA Examination this licensing option requires completion of a baccalaureate degree with a minimum of 120 units of education and two years of experience. Section 5093 requires exam passage, a baccalaureate degree and completion of additional units to total 150, and completion of one year of experience. CPAs meeting these licensure requirements are deemed to be substantially equivalent by NASBA. Law changes enacted at that time also eliminated the requirement that all applicants for licensure complete attest experience. Instead, 500 hours of attest experience are required to sign attest reports.

In the fall of 2003, the Board began considering the second component of substantial equivalency – cross-border practice. To address this matter, the UAA Task Force was appointed. The Task Force held four meetings during the winter and spring of 2003-2004, and in May of 2004, recommended the practice privilege law changes to the Board. These meetings of the Task Force provided a forum for extensive comment and input from representatives of the profession and from the Center for Public Interest Law.

The Task Force's deliberations lead to the identification of two key weaknesses in the temporary/incidental practice law that was then in effect: because the terms "temporary" and "incidental" were not defined in statute or regulation, there were wide differences in the way the terms were interpreted and applied. A second weakness was that, while anecdotal evidence suggested temporary/incidental practice was commonplace, the number and identity of practitioners entering the state in this way were largely unknown to the Board.

The Practice Privilege Program proposed by the Task Force was designed to address these weakness and also to facilitate cross-border practice. The statutory framework for this program was approved by the Board in May 2004 and enacted into law by SB 1543 (Figueroa, Chapter 921, Statutes of 2004) (see Attachment 1 for the text of the practice privilege laws).

The Practice Privilege Program allows an out-of-state CPA to qualify for cross-border practice in California by a process similar to the two methods provided for in the UAA or by having continually practiced public accountancy under a valid CPA license for at least four of the last ten years. The "four-of-ten provision" was intended to broaden the Board's requirements so that more out-of-state CPAs could qualify for practice privilege.

The program permits qualified out-of-state CPAs to begin practice upon the submission of the notification form, which can be done online. The program requires the out-of-state CPA to provide basic identifying information and to consent to the Board's jurisdiction. Unlike the UAA, these statutes give the Board the authority to immediately suspend the practice privilege of anyone who runs afoul of the practice privilege notification requirements or applicable laws. The program also differs from the UAA in that it specifies "disqualifying conditions" such as conviction of a crime or suspension of a license by another state. These conditions require prior Board approval before practice under a practice privilege can occur. Also, the Board's program provides for a fee to cover the cost of the program.

After putting forward its proposal for the Practice Privilege Program, the Task Force, renamed the Practice Privilege Task Force, began in July 2004 to develop the implementing regulations. Using the same process that was used to develop the statutory framework, the Task Force received extensive input from representatives of the profession and from the Center for Public Interest Law. The Task Force's policy recommendations were approved by the Board in September and November of 2004, and in January 2005 draft regulations were reviewed by the Board and scheduled for

public hearing. The public hearing took place in May 2005, and the regulations became operative on January 1, 2006, to coincide with the effective date of the statutes. No formal public comments were received during the rulemaking process.

At its meeting of May 19, 2005, one of the last actions of the Practice Privilege Task Force was to recommend Board approval of the list of substantially equivalent states. The Task Force's recommendation, which was adopted by the Board the next day, was to approve NASBA's current list of substantially equivalent states and to delegate the responsibility to the Executive Officer to revise the list as necessary. Attachment 2 provides a copy of the list.

DISCUSSION:

The Board has recently become aware that there are CPAs lawfully practicing in other states who would like to practice under a practice privilege but cannot qualify because they do not meet any of the three requirements for practice privilege specified in subdivision (a) of Business and Professions Code Section 5096: they are not from a state that is designated substantially equivalent; they do not individually meet the substantial equivalency requirements; and they do not qualify under "four of ten." It has been suggested that these requirements are a barrier that unnecessarily restricts the cross-border movement by qualified practitioners.

In evaluating the scope of the problem, is should be noted that 47 of the 55 states/jurisdictions are deemed by NASBA to be substantially equivalent. However, the remaining states/jurisdictions including Colorado and Florida do not meet the criteria for substantial equivalency. The primary reason some states are not deemed substantially equivalent is because they do not have the 150-Hour Requirement. As discussed above, while Section 5093 includes the 150-Hour Requirement, the Board continues to license CPAs who do not meet this requirement and only complete 120 units and a baccalaureate degree.

The fourth edition of the UAA (December 2005) acknowledged that not all states have enacted the 150 Hour Requirement and, in an effort to allow more time for transition, modified the start date of when 150 hours of education would be required for individual substantial equivalency. While the third edition of the UAA required 150 hours of education to qualify for individual substantial equivalency commencing on January 1, 2001, revised Section 23 in the fourth edition moves that date out to January 1, 2012 (see Attachment 3).

B. FIRM REGISTRATION REQUIREMENTS

ISSUE:

In January 2006, new laws establishing practice privilege became operative and the provision that had previously permitted temporary/incidental practice by accounting

practitioners from other states or foreign countries was repealed (see Attachment 4). Before its repeal, this provision had provided a mechanism that permitted practitioners from other states to practice temporarily on behalf of their firms in California. Under current law, qualified individual practitioners can practice in California under a practice privilege. To practice on behalf of the firm, the firm is required to be registered in California. Concerns have been raised that this requirement is creating a barrier to cross-border practice.

RELEVANT PROVISIONS OF THE ACCOUNTANCY ACT:

California law permits accountancy firms to be organized and registered by the Board as either partnerships (included limited liability partnerships or LLPs) or as accountancy professional corporations. Both partnerships and accountancy professional corporations may have nonlicensees as minority owners (Business and Professions Code Section 5079). California law does not permit accountancy firms to be organized as limited liability companies (LLCs).

California licensed CPAs and PAs may also practice as sole proprietors. There is no registration requirement for sole proprietors. If the sole proprietor chooses to practice under a fictitious name, Business and Professions Code Section 5060 requires that the name be neither false nor misleading. (See Attachment 5 for the text of Section 5060.)

Sections 5072 and 5073 of the Business and Professions Code specify the registration requirements for partnerships. The presence of at least one California partner is required for registration. If the partnership chooses to organize as an LLP, approval from the Office of the Secretary of State must be obtained before filing a partnership application with the Board. If the firm maintains an office in this state, there are additional requirements. (See Attachment 5 for relevant provisions of the Business and Professions Code.)

There are similar requirements for accountancy corporations which are specified in Sections 5150-5158 of the Business and Professions Code. The articles of incorporation must be endorsed and approved by the Secretary of State before the accountancy corporation may be registered by the Board. (See Attachment 5 for relevant provisions of the Business and Professions Code.)

The Corporations Code contains a number of provisions specific to partnerships, limited liability partnerships, and professional corporations. Accountancy firms must comply with all relevant legal requirements.

HISTORY AND BACKGROUND:

At the March 17, 2005, Practice Privilege Task Force meeting, the discussion of the draft FAQs related to Practice Privilege stimulated a discussion of firm registration. (See Attachment 6 for excerpts from the minutes of that meeting.) At that meeting, Enforcement Program Chief, Greg Newington stated that "if a firm practices public

accountancy through its agent – either a licensed or unlicensed individual – physically entering California or through servicing California clients, this is practicing public accountancy as defined in Section 5051 and the firm needs to be registered." During the discussion, it was also noted that most financial statement reports issued by licensees and most tax returns prepared by licensees are signed with the firm name.

Participants at the March 17, 2005, meeting noted that problems could arise because the practice privilege provisions provide for cross-border practice by individuals, but contain no comparable provisions for firms. It was further suggested that, while an exact number is unknown, some firms have been practicing public accountancy under the temporary practice provision in Section 5050 which would no longer be operative after December 31, 2005. This law change would not impact sole proprietors in other states since they would be able to render services under practice privilege. However, small firms could face significant problems due to the partner and shareholder licensing requirements in place for firm registration.

After this discussion, the Practice Privilege Task Force concluded that the issue needed further consideration, and a working group was appointed to develop a proposal for consideration at the May 2005 meetings of the Practice Privilege Task Force and the Board.

The working group evaluated the possibility of a practice privilege for firms and an expedited procedure for qualifying firms for registration and concluded that because of the numerous statutory requirements outside the Business and Professions Code that tie to registered firms, neither of these two options was practical. Because the greatest concern in this area was expressed by tax practitioners, the working group recommended a narrow exception from the firm registration requirement in the area of tax work for individuals (referred to in the statute as "natural persons").

This exception was drafted as Business and Professions Code Section 5054 and considered by the Practice Privilege Task Force and Board at their May 2005 meetings. Discussion at the Task Force meeting indicated that proposed Section 5054 addressed the primary concerns related to practice privilege as expressed by tax practitioners. Task Force members suggested some edits to the language. (See Attachment 7 for excerpts from the minutes of that meeting.)

This matter was considered by the Board the next day. Minutes of that meeting state the following regarding the working group's activities as reported by the Task Force chair, Gail Hillebrand: "Ms. Hillebrand noted that there were a number of very serious issues that were considered by the working group. They noted that registered firms have a variety of obligations and it would be inappropriate for these obligations to be waived simply because the individual held the practice privilege."

Minutes of the meeting further indicate members of the public and representatives of the profession communicated no opposition or concern to the Task Force's

recommendation which was unanimously approved by all Board members present. (See Attachment 8 for excerpts from the minutes of that meeting.)

Section 5054 was included in SB 229 by Senator Figueroa and enacted in 2005 (Chapter 658, statutes of 2005). Section 5054 reads:

> 5054. (a) Notwithstanding any other provision of this chapter, an individual or firm holding a valid and current license, certificate, or permit to practice public accountancy from another state may prepare tax returns for natural persons who are California residents or estate tax returns for the estates of natural persons who were clients at the time of death without obtaining a permit to practice public accountancy issued by the board under this chapter or a practice privilege pursuant to Article 5.1 (commencing with Section 5096) provided that the individual or firm does not physically enter California to practice public accountancy pursuant to Section 5051, does not solicit California clients, and does not assert or imply that the individual or firm is licensed or registered to practice public accountancy in California.
>
> (b) The board may, by regulation, limit the number of tax returns that may be prepared pursuant to subdivision (a).

While Section 5054 addressed some concerns, problems related to firm registration remain as indicated in the February 6, 2006, letter from the California Society of Certified Public Accountants (CalCPA) (Attachment 9).

DISCUSSION:

Concern has recently been expressed regarding the scope of Section 5054. The exception contained in that section is very narrow, and many types of tax returns commonly prepared by CPAs such as partnership or corporate tax returns are excluded. It has been suggested that, because of this, smaller firms that are not registered in California may still find it difficult to serve clients in this state and may find it difficult to compete with others such as enrolled agents and tax preparers who are providing similar tax services. It has also been suggested that other states may retaliate by enacting similar laws that restrict the cross-border practice of California CPA firms.

To provide services beyond the scope of Section 5054 under current law, the out-of-state firm must be registered in California. The firm is required to have a California licensee as a partner or shareholder. Also, the firm must pay a firm registration application fee ($150) and a fee for the firm's initial permit to practice ($200). These requirements may be challenging for some firms. Another difficulty may occur because in many instances the out-of-state firm is organized in a way that is not permitted under California law. For example, California law does not permit limited liability companies (LLCs) to practice public accounting. Even if these challenges are overcome, the registration process itself can be time-consuming. It takes, on the average, six to eight weeks for the Board to process the registration application. Also, if the firm elects to operate as a limited liability partnership or a professional corporation, approval from the

Office of the Secretary of State is necessary before making application to the Board, and this adds additional time and expense to the application process.

Issues related to Section 5054 are different for California-registered firms. For California-registered firms, legal counsel has advised that the exception contained in Section 5054 does not apply. By virtue of being registered, the firm has a presence in this state and is therefore ineligible for the Section 5054 exception (see Attachment 10). This can pose a problem for the out-of-state licensees employed by these firms who are involved in the preparation of tax returns for California residents. This problem is discussed in the February 2, 2006, letter to Ronald Blanc, Esq. and Gail Hillebrand, Esq. by Richard Robinson (Attachment 11, pages 2 -5).

C. WHAT CONSTITUTES A CALIFORNIA CLIENT

ISSUE:

In 2005 as planning for practice privilege implementation was underway, an attempt was made to establish a bright-line test to identify when a practice privilege was needed. Consistent with the Board's historic practice, it was determined that if the out-of-state CPA physically enters California to provide public accounting services or if the CPA provides services to California clients, a practice privilege (or a California license) would be needed. Concern has been expressed that the second standard – servicing a California client – cannot be used as a bright line test, primarily because it is unclear what constitutes a California client.

RELEVANT PROVISIONS IN THE ACCOUNTANCY ACT

Business and Professions Code Section 5035.2 provides a definition of "client." Section 5050 requires a valid permit to practice to practice public accountancy in this state. Section 5051 provides a definition of the practice of public accountancy. (See Attachment 12 for the text of these statutes.)

HISTORY AND BACKGROUND:

As part of the implementation of the Practice Privilege Program, staff developed FAQs to address basic questions related to the program. One of the issues considered by staff in developing these FAQs was when a practice privilege would be needed. The FAQs were discussed at the March 17, 2005, meeting of the Practice Privilege Task Force. At that meeting Greg Newington, Enforcement Program Chief, explained the efforts of staff to develop a bright-line test regarding when a practice privilege was needed. The minutes of that meeting indicate Mr. Newington stated the following: (Attachment 6):

> The intent was to establish a bright-line test related to practice privilege. He explained that, as staff went through the various scenarios, the test was if the individual physically comes into California to perform the activities in subdivisions

(a) – (f) of Section 5051 or services California clients from outside the state, this is practicing public accounting in California.

The discussion at the March 17, 2005, meeting then moved on to concerns regarding firm registration. The issue of what constitutes a California client was not further addressed at that time. The issue recently re-emerged and was discussed at length in the February 2, 2006, letter from Richard Robinson to Ronald Blanc, Esq., and Gail K. Hillebrand, Esq. (see Attachment 11, page 5-8).

DISCUSSION:

As discussed above, when staff began the process of developing practice privilege FAQs, an effort was made to create a bright-line test to identify when a practice privilege is needed. For this purpose two criteria were identified: 1) when the practitioner physically enters the state or 2) when services were provided to a California client. In preparation for the February 22, 2006, meeting these criteria were reconsidered, and a lack of clarity regarding what constitutes a California client led staff to seek advice from legal counsel.

Legal counsel clarified that the practice of public accountancy is defined in Section 5051 in terms of services not in terms of who is the client. When these services are provided in California, it is the practice of public accounting in California. While on the face of it might appear that the "practice in this state" is based on the physical location of the practitioner while he or she is working on the public accounting engagement, that is not necessarily the case. Consequently, physical presence in this state may not be an appropriate guideline. Instead, legal counsel has indicated that a primary guideline is that there must be a clear connection with California, and the determination that the services were performed in California must be based on the facts and circumstances of the particular engagement.

Using this guideline, some activities clearly appear to be the practice of public accountancy in California:

- A CPA solicits business by offering to prepare California tax returns and then, as a result of that solicitation, prepares a California tax return for an individual person (legally referred to as a "natural person") residing in California.

- The CPA performs an audit of a California school district.

- The CPA prepares a compilation for a small business with operations solely in California.

Application of this approach proves challenging when the client is a business with operations in multiple states and/or in foreign countries. In such instances it is not a simple matter to analyze the relevant facts and circumstances to make a determination regarding whether service to such a client constitutes the practice of public accounting

in California. This complexity is well illustrated by the memo from George P. Ritter, DCA Staff Counsel, to Carol Sigmann (agenda item III.D). Even if the CPA is willing and able to disclose to the Board all of the relevant facts and circumstances of the engagement (which is highly unlikely), Board practice privilege and licensing staff would still lack adequate legal knowledge and adequate time to make a such a complex determination. Such a case-by-case review by staff for these programs is simply a practical impossibility. In sum, it does not appear possible to create a bright-line test that can easily be applied by Board staff.

It should be noted that this problem is not new. The law defining the practice of public accountancy was not modified when practice privilege was enacted. It is likely that in the past this problem did not present itself because so many activities could be folded in under the rubric of "temporary practice." However, enactment of the practice privilege provisions and repeal of temporary practice brought this matter to the forefront.

CONCLUSION

To evaluate these issues, staff did extensive research and held lengthy discussions with legal counsel. These discussions generated a number of ideas for possible statute changes to address the problems that were identified: a new law providing for interim practice by out-of-state firms, the amendment of Section 5054 so that the exception would apply to tax returns prepared for entities such as partnerships and corporations as well as for natural persons, the amendment of Section 5054 so that the exception would apply to employees of California registered firms; a new temporary practice law for both individuals and firms that would clarify what constitutes temporary practice; a new temporary practice law that would only apply to non-attest work, and an amendment to the practice privilege laws to allow any CPA with a current, valid, active license without disqualifying conditions (not just those with 150 hours of education) to immediately qualify for practice privilege.

After extensive discussion, it was concluded that none of these concepts were sufficiently developed to be recommended as a solution to the complex problems discussed above. Effectively addressing such complex issues requires a deliberative process in a public forum with input from all interested parties, and this cannot be accomplished in a one-day meeting. On the other hand, the needs of practitioners and their clients appear urgent. With this in mind, the following approach is offered for CPC and Board consideration:

- Amend Section 5050 to add language similar to the temporary/incidental practice language that was repealed effective January 1, 2006, with an express reference to firms and a sunset date to be determined by the Board. Although there are identified weaknesses with this language, it has stood the test of time, and reinstating it for a short period of time will give the Board the opportunity to further study the issues and craft a practical solution. This appears better than a quickly drafted piecemeal approach which could have unintended consequences creating

more problems than it solves. (See Attachment 4 for the text of the repealed language.)

- Keep the basic practice privilege provisions in place to facilitate compliance by firms with the Sarbanes-Oxley Act and the audit partner rotation requirements.

- Make conforming amendments to other statutes for consistency.

If this general approach is approved by the Board, the following questions would need to be addressed so that language could be drafted:

- What should be the sunset date?

  The time frame for this work would be defined by the sunset date in the legislation. From a practical standpoint, it appears that the shortest time frame for addressing this matter and pursuing legislation would be around two years. This would mean a 2009 sunset date so that new legislation can be introduced and enacted in 2008. Another option would be to set the sunset date at January 1, 2011, to coincide with the sunset date for the Practice Privilege Program so that these issues can be addressed as part of evaluating the program.

  The shorter time period may minimize any risk to consumers that could result from permitting temporary/interim practice that is largely outside the Board's oversight. As discussed above, concerns in this area were one reason the Board began to develop the practice privilege program. On the other hand, in the past there have been very few consumer complaints specific to work occurring under the temporary/interim practice provision. In addition, if this approach goes forward, the Board may want to add consumer information to its Web site, similar to the consumer information on Internet practice, clarifying for consumers the risks of using practitioners that do not have a license or a practice privilege in this state.

- Should the Board continue going forward with the foreign temporary practice provision as it was adopted at the January 2006 meeting?

  The repealed language formerly in Section 5050 covered both accountants from other states and accountants from other countries. However, it is more broadly crafted than the language approved in January which required that the foreign accountant's temporary practice be performed under the accounting or auditing standards of the foreign country (see Attachment 13.) It is possible to have separate provisions that apply only to foreign practitioners. CPAs licensed by other U.S. states or jurisdictions have met licensing requirements similar to the requirements for the California license, including passage of the Uniform CPA Examination. Also, CPAs in the U.S. all perform work under the same accounting and auditing standards. On the other hand, the credentialing requirements and standards of practice in foreign countries are different from California's.

- Should Section 5088 be amended to allow all out-of-state CPAs applying for a California license to practice while their licensing applications are pending?

  Prior to January 1, 2006, all out-of-state CPAs applying for a California license could practice under the language previously in Section 5088 (See Attachment 14). Currently, they are required to submit a notification and obtain a practice privilege in order to practice (even though they have already provided the Board with the same information on their applications for licensure). CPAs applying with 150 units of education are able to qualify for practice privilege. However, as noted above, the Board also licenses people who have 120 units of education. CPAs in this group can qualify for licensure, but cannot qualify for practice privilege unless they are able to qualify under the "four of ten" provision. Reinstating the language previously in Section 5088 would permit these CPAs to practice while their California licensure applications are pending, a time period that averages approximately six to eight weeks. Enacting a provision similar to the temporary/incidental practice language previously in Section 5050 may not be adequate to address the needs of this group of CPAs since they are applying for a California license which suggests they have an interest that goes beyond temporary/incidental practice and that they intend to establish a permanent presence in this state.

If the CPC elects to go forward with the approach outlined above, statutory language could be prepared for Board consideration February 23, 2006.

BUSINESS AND PROFESSIONS CODE SECTIONS 5096-5096.11

5096. (a) An individual whose principal place of business is not in this state and who has a valid and current license, certificate or permit to practice public accountancy from another state may, subject to the conditions and limitations in this article, engage in the practice of public accountancy in this state under a practice privilege without obtaining a certificate or license under this chapter if the individual satisfies one of the following:

(1) The individual has continually practiced public accountancy as a certified public accountant under a valid license issued by any state for at least four of the last ten years.

(2) The individual has a license, certificate, or permit from a state which has been determined by the board to have education, examination, and experience qualifications for licensure substantially equivalent to this state's qualifications under Section 5093.

(3) The individual possesses education, examination, and experience qualifications for licensure which have been determined by the board to be substantially equivalent to this state's qualifications under Section 5093.

(b) The board may designate states as substantially equivalent under paragraph (2) of subdivision (a) and may accept individual qualification evaluations or appraisals conducted by designated entities, as satisfying the requirements of paragraph (3) of subdivision (a).

(c) To obtain a practice privilege under this section, an individual who meets the requirements of subdivision (a), shall do the following:

(1) In the manner prescribed by board regulation, notify the board of the individual's intent to practice.

(2) Pay a fee as provided in Article 8 (commencing with Section 5130).

(d) Except as otherwise provided by this article or by board regulation, the practice privilege commences when the individual notifies the board, provided the fee is received by the board within 30 days of that date. The board shall permit the notification to be provided electronically.

(e) An individual who holds a practice privilege under this

article:

(1) Is subject to the personal and subject matter jurisdiction and disciplinary authority of the board and the courts of this state.

(2) Shall comply with the provisions of this chapter, board regulations, and other laws, regulations, and professional standards applicable to the practice of public accountancy by the licensees of this state and to any other laws and regulations applicable to individuals practicing under practice privileges in this state except the individual is deemed, solely for the purpose of this article, to have met the continuing education requirements and ethics examination requirements of this state when such individual has met the examination and continuing education requirements of the state in which the individual holds the valid license, certificate, or permit on which the substantial equivalency is based.

(3) Shall not provide public accountancy services in this state from any office located in this state, except as an employee of a firm registered in this state. This paragraph does not apply to public accountancy services provided to a client at the client's place of business or residence.

(4) Is deemed to have appointed the regulatory agency of the state that issued the individual's certificate, license, or permit upon which substantial equivalency is based as the individual's agent on whom notices, subpoenas or other process may be served in any action or proceeding by the board against the individual.

(5) Shall cooperate with any board investigation or inquiry and shall timely respond to a board investigation, inquiry, request, notice, demand or subpoena for information or documents and timely provide to the board the identified information and documents.

(f) A practice privilege expires one year from the date of the notice, unless a shorter period is set by board regulation.

(g) (1) No individual may practice under a practice privilege without prior approval of the board if the individual has, or acquires at any time during the term of the practice privilege, any disqualifying condition under paragraph (2) of this subdivision.

(2) Disqualifying conditions include:

(A) Conviction of any crime other than a minor traffic violation.

(B) Revocation, suspension, denial, surrender or other discipline or sanctions involving any license, permit, registration, certificate or other authority to practice any profession in this or any other state or foreign country or to practice before any state, federal, or local court or agency, or the Public Company Accounting Oversight Board.

(C) Pendency of any investigation, inquiry or proceeding by or before any state, federal or local court or agency, including, but not limited to, the Public Company Accounting Oversight Board,

involving the professional conduct of the individual.

(D) Any judgment or arbitration award against the individual involving the professional conduct of the individual in the amount of thirty thousand dollars ($30,000) or greater.

(E) Any other conditions as specified by the board in regulation.

(3) The board may adopt regulations exempting specified minor occurrences of the conditions listed in subparagraph (B) of paragraph (2) from being disqualifying conditions under this subdivision.

5096.1. (a) Any individual, not a licensee of this state, who is engaged in any act which is the practice of public accountancy in this state, and who has not given notice of intent to practice under practice privileges and paid the fee required pursuant to the provisions of this article, and who has a license, certificate or other authority to engage in the practice of public accountancy in any other state, regardless of whether active, inactive, suspended, or subject to renewal on payment of a fee or completion of an educational or ethics requirement, is:

(1) Deemed to be practicing public accountancy unlawfully in this state.

(2) Subject to the personal and subject matter jurisdiction and disciplinary authority of the board and the courts of this state to the same extent as a holder of a valid practice privilege.

(3) Deemed to have appointed the regulatory agency of the state that issued the individual's certificate or license as the individual' s agent on whom notice, subpoenas, or other process may be served in any action or proceeding by the board against the individual.

(b) The board may prospectively deny a practice privilege to any individual who has violated this section or implementing regulations or committed any act which would be grounds for discipline against the holder of a practice privilege.

5096.2. (a) Practice privileges may be denied for failure to qualify under or comply with the provisions of this article or implementing regulations, or for any act that if committed by an applicant for licensure would be grounds for denial of a license under Section 480 or if committed by a licensee would be grounds for discipline under Section 5100, or for any act committed outside of this state that would be a violation if committed within this state.

(b) The board may deny practice privileges using either of the following procedures:

(1) Notifying the individual in writing of all of the following:
(A) That the practice privilege is denied.
(B) The reasons for denial.
(C) The earliest date on which the individual is eligible for a practice privilege.
(D) That the individual has a right to appeal the notice and request a hearing under the provisions of the Administrative Procedure Act if a written notice of appeal and request for hearing is made within 60 days.
(E) That, if the individual does not submit a notice of appeal and request for hearing within 60 days, the board's action set forth in the notice shall become final.
(2) Filing a statement of issues under the Administrative Procedure Act.
(c) An individual who had been denied a practice privilege may apply for a new practice privilege not less than one year after the effective date of the notice or decision denying the practice privilege unless a longer time period, not to exceed three years, is specified in the notice or decision denying the practice privilege.

5096.3. (a) Practice privileges are subject to revocation, suspension, fines or other disciplinary sanctions for any conduct that would be grounds for discipline against a licensee of the board or for any conduct in violation of this article or regulations implementing this article.
(b) Practice privileges are subject to discipline during any time period in which they are valid, under administrative suspension, or expired.
(c) The board may recover its costs pursuant to Section 5107 as part of any disciplinary proceeding against the holder of a practice privilege.
(d) An individual whose practice privilege has been revoked may apply for a new practice privilege not less than one year after the effective date of the board's decision revoking the individual's practice privilege unless a longer time period, not to exceed three years, is specified in the board's decision revoking the practice privilege.
(e) The provisions of the Administrative Procedure Act, including, but not limited to, the commencement of a disciplinary proceeding by the filing of an accusation by the board shall apply under this article.

5096.4. (a) The right of an individual to practice in this state under a practice privilege may be administratively suspended at any time by an order issued by the board or its executive officer, without prior notice or hearing, for the purpose of conducting a disciplinary investigation, proceeding, or inquiry concerning the representations made in the notice, the individual's competence or qualifications to practice under practice privileges, failure to timely respond to a board inquiry or request for information or documents, or under other conditions and circumstances provided for by board regulation.

(b) The administrative suspension order is immediately effective when mailed to the individual's address of record or agent for notice and service as provided for in this article.

(c) The administrative suspension order shall contain the following:

(1) The reason for the suspension.

(2) A statement that the individual has the right, within 30 days, to appeal the administrative suspension order and request a hearing.

(3) A statement that any appeal hearing will be conducted under the provisions of the Administrative Procedure Act applicable to individuals who are denied licensure, including the filing of a statement of issues by the board setting forth the reasons for the administrative suspension of practice privileges and specifying the statutes and rules with which the individual must show compliance by producing proof at the hearing and in addition any particular matters that have come to the attention of the board and that would authorize the administrative suspension, or the denial of practice privileges.

(d) The burden is on the holder of the suspended practice privilege to establish both qualification and fitness to practice under practice privileges.

(e) The administrative suspension shall continue in effect until terminated by an order of the board or the executive officer or expiration of the practice privilege under administrative suspension.

(f) Administrative suspension is not discipline and shall not preclude any individual from applying for a license to practice public accountancy in this state or from applying for a new practice privilege upon expiration of the one under administrative suspension, except that the new practice privilege shall not be effective until approved by the board.

(g) Notwithstanding any administrative suspension, a practice privilege expires one year from the date of notice unless a shorter period is set by board regulation.

(h) Proceedings to appeal an administrative suspension order may

be combined or coordinated with proceedings for denial or discipline of a practice privilege.

5096.5. Notwithstanding any other provision of this article, an individual may not sign any attest report pursuant to a practice privilege unless the individual meets the experience requirements of Section 5095 and completes any continuing education or other conditions required by the board regulations implementing this article.

5096.6. In addition to the authority otherwise provided for by this code, the board may delegate to the executive officer the authority to issue any notice or order provided for in this article and to act on behalf of the board, including, but not limited to, issuing a notice of denial of a practice privilege and an interim suspension order, subject to the right of the individual to timely appeal and request a hearing as provided for in this article.

5096.7. Except as otherwise provided in this article, the following definitions apply:

(a) Anywhere the term "license," "licensee," "permit," or "certificate" is used in this chapter or Division 1.5 (commencing with Section 475), it shall include persons holding practice privileges under this article, unless otherwise inconsistent with the provisions of the article.

(b) Any notice of practice privileges under this article and supporting documents is deemed an application for licensure for purposes of the provisions of this code, including, but not limited to, the provisions of this chapter and the provisions of Division 1.5 (commencing with Section 475) related to the denial, suspension and revocation of licenses.

(c) Anywhere the term "employee" is used in this article it shall include, but is not limited to, partners, shareholders, and other owners.

5096.8. In addition to the authority otherwise provided by this code, all investigative powers of the board, including those delegated to the executive officer, shall apply to investigations concerning compliance with, or actual or potential violations of, the provisions of this article or implementing regulations, including,

but not limited to, the power to conduct investigations and hearings by the executive officer under Section 5103 and to issuance of subpoenas under Section 5108.

5096.9. The board is authorized to adopt regulations to implement, interpret, or make specific the provisions of this article.

5096.10. The provisions of this article shall only be operative if commencing July 1, 2005, and continuing during the period provided in Section 5096.11, there is an appropriation from the Accountancy Fund in the annual Budget Act to fund the activities in the article and sufficient hiring authority is granted pursuant to a budget change proposal to the board to provide staffing to implement this article.

5096.11. This article shall become operative on January 1, 2006. It shall remain in effect only until January 1, 2011, and as of that date is repealed, unless a later enacted statute, which becomes effective on or before January 1, 2011, deletes or extends that date.

BUSINESS AND PROFESSIONS CODE SECTIONS 5088 AND 5093

5088. (a) Any individual who is the holder of a current and valid license as a certified public accountant issued under the laws of any state and who applies to the board for a license as a certified public accountant under the provisions of Section 5087 may, until the time the application for a license is granted or denied, practice public accountancy in this state only under a practice privilege pursuant to the provisions of Article 5.1 (commencing with Section 5096), except that, for purposes of this section, the individual is not disqualified from a practice privilege during the period the application is pending by virtue of maintaining an office or principal place of business, or both, in this state. The board may by regulation provide for exemption, credit, or proration of fees to avoid duplication of fees.

(b) This section shall become operative on January 1, 2006.

5093. (a) To qualify for the certified public accountant license, an applicant who is applying under this section shall meet the education, examination, and experience requirements specified in subdivisions (b), (c), and (d), or otherwise prescribed pursuant to this article. The board may adopt regulations as necessary to implement this section.

(b) (1) An applicant for admission to the certified public accountant examination under the provisions of this section shall present satisfactory evidence that the applicant has completed a baccalaureate or higher degree conferred by a college or university, meeting, at a minimum, the standards described in Section 5094, the total educational program to include a minimum of 24 semester units in accounting subjects and 24 semester units in business related subjects. This evidence shall be provided at the time of application for admission to the examination, except that an applicant who applied, qualified, and sat for at least two subjects of the examination for the certified public accountant license before May 15, 2002, may provide this evidence at the time of application for licensure.

(2) An applicant for issuance of the certified public accountant

license under the provisions of this section shall present satisfactory evidence that the applicant has completed at least 150 semester units of college education including a baccalaureate or higher degree conferred by a college or university, meeting, at a minimum, the standards described in Section 5094, the total educational program to include a minimum of 24 semester units in accounting subjects and 24 semester units in business related subjects. This evidence shall be presented at the time of application for the certified public accountant license.

(c) An applicant for the certified public accountant license shall pass an examination prescribed by the board.

(d) The applicant shall show, to the satisfaction of the board, that the applicant has had one year of qualifying experience. This experience may include providing any type of service or advice involving the use of accounting, attest, compilation, management advisory, financial advisory, tax or consulting skills. To be qualifying under this section, experience shall have been performed in accordance with applicable professional standards. Experience in public accounting shall be completed under the supervision or in the employ of a person licensed or otherwise having comparable authority under the laws of any state or country to engage in the practice of public accountancy. Experience in private or governmental accounting or auditing shall be completed under the supervision of an individual licensed by a state to engage in the practice of public accountancy.

Appendix 1

Substantially Equivalent States

The following 46 jurisdictions have CPA licensure requirements that are deemed by the California Board of Accountancy to be substantially equivalent to California's licensure requirements. Pursuant to Section 27 of Title 16, Article 4 of the California Code of Regulations, you are authorized to practice public accountancy in California under the practice privilege provisions if you hold a valid, current license from a state identified below, unless you check "Y" to any of the disqualifying conditions on the Notification Form. Please see the instructions to the Notification Form for additional information.

Alabama*
Alaska
Arizona
Arkansas
Connecticut
District of Columbia*
Georgia
Guam
Hawaii
Idaho
Illinois*
Indiana
Iowa*
Kansas*
Kentucky
Louisiana*
Maine
Maryland
Massachusetts
Michigan
Minnesota
Mississippi
Missouri*
Montana*
Nebraska*
Nevada
New Jersey
New Mexico
New York
North Carolina
North Dakota
Ohio
Oklahoma
Oregon
Pennsylvania
Rhode Island
South Carolina
South Dakota*
Tennessee
Texas
Utah
Virginia
Washington*
West Virginia*
Wisconsin
Wyoming*

* Permit Holders Only

SECTION 23
SUBSTANTIAL EQUIVALENCY

(a)(1) An individual whose principal place of business is not in this state having a valid certificate or license as a Certified Public Accountant from any state which the NASBA National Qualification Appraisal Service has verified to be in substantial equivalence with the CPA licensure requirements of the AICPA/NASBA Uniform Accountancy Act shall be presumed to have qualifications substantially equivalent to this state's requirements and shall have all the privileges of certificate holders and licensees of this state without the need to obtain a certificate or permit under Sections 6 or 7. However, such individuals shall notify the Board of their intent to enter the state under this provision.

(2) An individual whose principal place of business is not in this state having a valid certificate or license as a Certified Public Accountant from any state which the NASBA National Qualification Appraisal Service has not verified to be in substantial equivalence with the CPA licensure requirements of the AICPA/NASBA Uniform Accountancy Act shall be presumed to have qualifications substantially equivalent to this state's requirements and shall have all the privileges of certificate holders and licensees of this state without the need to obtain a certificate or permit under Sections 6 or 7 if such individual obtains from the NASBA National Qualification Appraisal Service verification that such individual's CPA qualifications are substantially equivalent to the CPA licensure requirements of the AICPA/NASBA Uniform Accountancy Act. However, such individuals shall notify the Board of their intent to enter the state under this provision. Any individual who passed the Uniform CPA Examination and holds a valid license issued by any other state prior to January 1, 2012 may be exempt from the education requirement in Section 5(c)(2) for purposes of this Section 23 (a)(2).

(3) Any licensee of another state exercising the privilege afforded under this section hereby consents, as a condition of the grant of this privilege:

(a) to the personal and subject matter jurisdiction and disciplinary authority of the Board,

(b) to comply with this Act and the Board's rules; and,

(c) to the appointment of the State Board which issued their license as their agent upon whom process may be served in any action or proceeding by this Board against the licensee.

COMMENT: Subsection 23(a)(3) is intended to allow state boards to discipline licensees from other states that practice in their state. Under Section 23(a), State Boards could utilize the NASBA National Qualification Appraisal Service for determining whether another state's certification criteria are "substantially equivalent" to the national standard outlined in the AICPA/NASBA Uniform Accountancy Act. If a state is determined to be "substantially equivalent," then individuals from that state would have ease of practice rights in other states.

Individuals who personally meet the substantial equivalency standard may also apply to the National Qualification Appraisal Service if the state in which they are licensed is not substantially equivalent to the UAA.

Individual CPAs who practice across state lines or who service clients in another state via electronic technology, would not be required to obtain a reciprocal certificate or license if their state of original certification is deemed substantially equivalent, or if they are individually deemed substantially equivalent. Under Section 23, the CPA merely must notify the Board of the state in which the service is being performed. However, licensure is required in the state where the CPA has their principal place of business. If a CPA relocates to another state and establishes their principal place of business in that state then they would be required to obtain a certificate in that state. See Section 6(c)(2). Likewise, if a firm opens an office in a state they would be required to obtain a license in that state. See also Sections 7(i) and 7(j) which allow the use of substantial equivalency on a firm wide basis.

As it relates to the notification requirement, states should consider the need for such a requirement since the nature of an enforcement complaint would in any event require the identification of the CPA, and a CPA practicing on the basis of substantial equivalency will be subject to enforcement action in any state under Section 23 (a)(3) regardless of a notification requirement.

Implementation of the "'substantial equivalency" standard and creation of the National Qualification Appraisal Service will make a significant improvement in the current regulatory system and assist in accomplishing the goal of portability of the CPA title and mobility of CPAs across state lines.

In order to be deemed substantially equivalent under Section 23(a)(1), a state must adopt the 150-hour education requirement established in Section 5(c)(2). A few states have not yet implemented the education provision. In order to allow a reasonable transition period, Section 23(a)(2) provides that an individual who has passed the Uniform CPA examination and holds an active license from a state that is not yet substantially equivalent may be individually exempt from the 150-hour education requirement and may be allowed to use practice privileges in this state if the individual was licensed prior to January 1, 2012.

(b) **A licensee of this state offering or rendering services or using their CPA title in another state shall be subject to disciplinary action in this state for an act committed in another state for which the licensee would be subject to discipline for an act committed in the other state. Notwithstanding Section 11(a), the Board shall be required to investigate any complaint made by the board of accountancy of another state.**

COMMENT: This section ensures that the Board of the state of the licensee's principal place of business, which has power to revoke a license, will have the authority to discipline its licensees if they violate the law when performing services in other states and to ensure that the state board of accountancy will be required to give consideration to complaints made by the boards of accountancy of other jurisdictions.

5050. Practice Without Permit: Temporary Practice, Out-of-State Licensee (Operative until January 1, 2006) – *Repealed* –

(a) No person shall engage in the practice of public accountancy in this State unless such person is the holder of a valid permit to practice public accountancy issued by the board; provided, however, that nothing in this chapter shall prohibit a certified public accountant or a public accountant of another state, or any accountant of a foreign country lawfully practicing therein, from temporarily practicing in this State on professional business incident to his regular practice in another state or country.

(b) This section shall become in operative on January 1, 2006, and as of that date is repealed.

BUSINESS AND PROFESSIONS CODE SECTIONS 5060, 5072, 5073, 5078, and 5079

5060. (a) No person or firm may practice public accountancy under any name which is false or misleading.

(b) No person or firm may practice public accountancy under any name other than the name under which the person or firm holds a valid permit to practice issued by the board.

(c) Notwithstanding subdivision (b), a sole proprietor may practice under a name other than the name set forth on his or her permit to practice, provided the name is registered by the board, is in good standing, and complies with the requirements of subdivision (a).

(d) The board may adopt regulations to implement, interpret, and make specific the provisions of this section including, but not limited to, regulations designating particular forms of names as being false or misleading.

5072. (a) No persons shall engage in the practice of accountancy as a partnership unless the partnership is registered by the board.

(b) A partnership, other than a limited partnership, may be registered by the board to engage in the practice of public accountancy provided it meets the following requirements:

(1) At least one general partner shall hold a valid permit to practice as a certified public accountant, public accountant, or accountancy corporation, or shall be an applicant for a certificate as a certified public accountant under Sections 5087 and 5088.

(2) Each partner personally engaged within this state in the practice of public accountancy as defined by Section 5051 shall hold a valid permit to practice in this state or shall have applied for a certificate as a certified public accountant under Sections 5087 and 5088.

(3) Each partner not personally engaged in the practice of public accountancy within this state shall be a certified public accountant in good standing of some state, except as permitted by Section 5079.

(4) Each resident manager in charge of an office of the firm in this state shall be a licensee in good standing of this state, or shall have applied for a certificate as a certified public accountant under Sections 5087 and 5088.

5073. (a) Application for registration of a partnership shall be made upon a form prescribed by the board. The board shall in each case determine whether the applicant is eligible for registration.

(b) A partnership that is so registered and that holds a valid permit issued under this article and that has at least one general partner who is licensed to practice using the designation "certified public accountant" or the abbreviation "C.P.A." and one additional licensed person may use the words "certified public accountants" or the abbreviation"C.P.A.s" in connection with its partnership name.

(c) A partnership that is so registered and that holds a valid permit issued under this article and that has at least one general partner who is licensed to practice using the designation "public accountant" or the abbreviation "P.A." and one additional licensed person may use the words "public accountants" or the abbreviation "P.A.s" in connection with its partnership name.

(d) Notification shall be given to the board within one month after the admission to, or withdrawal of, a partner from any partnership so registered.

(e) Any registration of a partnership under this section granted in reliance upon Sections 5087 and 5088 shall terminate forthwith if the board rejects the application under Sections 5087 and 5088 of the general partner who signed the application for registration as a partnership, or any partner personally engaged in the practice of public accountancy in this state, or any resident manager of a partnership in charge of an office in this state.

5078. In each office of a certified public accountant or public accountant in this state which is not under the personal management of such an accountant, respectively, work shall be supervised by a certified public accountant or public accountant.

5079. (a) Notwithstanding any other provision of this chapter, any firm lawfully engaged in the practice of public accountancy in this state may have owners who are not licensed as certified public accountants or public accountants if the following conditions are met:

(1) Nonlicensee owners shall be natural persons or entities, such as partnerships, professional corporations, or others, provided that each ultimate beneficial owner of an equity interest in that entity shall be a natural person materially participating in the business

conducted by the firm or an entity controlled by the firm.

(2) Nonlicensee owners shall materially participate in the business of the firm, or an entity controlled by the firm, and their ownership interest shall revert to the firm upon the cessation of any material participation.

(3) Licensees shall in the aggregate, directly or beneficially, comprise a majority of owners, except that firms with two owners may have one owner who is a nonlicensee.

(4) Licensees shall in the aggregate, directly or beneficially, hold more than half of the equity capital and possess majority voting rights.

(5) Nonlicensee owners shall not hold themselves out as certified public accountants or public accountants and each licensed firm shall disclose actual or potential involvement of nonlicensee owners in the services provided.

(6) There shall be a certified public accountant or public accountant who has ultimate responsibility for each financial statement attest and compilation service engagement.

(7) Except as permitted by the board in the exercise of its discretion, a person may not become a nonlicensee owner or remain a nonlicensee owner if the person has done either of the following:

(A) Been convicted of any crime, an element of which is dishonesty or fraud, under the laws of any state, of the United States, or of any other jurisdiction.

(B) Had a professional license or the right to practice revoked or suspended for reasons other than nonpayment of dues or fees, or has voluntarily surrendered a license or right to practice with disciplinary charges or a disciplinary investigation pending, and not reinstated by a licensing or regulatory agency of any state, or of the United States, including, but not limited to, the Securities and Exchange Commission or Public Company Accounting Oversight Board, or of any other jurisdiction.

(b) (1) A nonlicensee owner of a licensed firm shall report to the board in writing of the occurrence of any of the events set forth in paragraph (7) of subdivision (a) within 30 days of the date the nonlicensee owner has knowledge of the event. A conviction includes the initial plea, verdict, or finding of guilt, pleas of no contest, or pronouncement of sentence by a trial court even though that conviction may not be final or sentence actually imposed until appeals are exhausted.

(2) A California nonlicensee owner of a licensed firm shall report to the board in writing the occurrence of any of the following events occurring on or after January 1, 2006, within 30 days of the date the California nonlicensee owner has knowledge of the events:

(A) Any notice of the opening or initiation of a formal investigation of the nonlicensee owner by the Securities and Exchange

Commission or its designee, or any notice from the Securities and Exchange Commission to a nonlicensee owner requesting a Wells submission.

(B) Any notice of the opening or initiation of an investigation of the nonlicensee owner by the Public Company Accounting Oversight Board or its designee.

(C) Any notice of the opening or initiation of an investigation of the nonlicensee owner by another professional licensing agency.

(3) The report required by paragraphs (1) and (2) shall be signed by the nonlicensee owner and set forth the facts that constitute the reportable event. If the reportable event involves the action of an administrative agency or court, the report shall identify the name of the agency or court, the title of the matter, and the date of occurrence of the event.

(4) Notwithstanding any other provision of law, reports received by the board pursuant to paragraph (2) shall not be disclosed to the public pursuant to the California Public Records Act (Chapter 3.5 (commencing with Section 6250) of Division 7 of Title 1 of the Government Code) other than (A) in the course of any disciplinary proceeding by the board after the filing of a formal accusation, (B) in the course of any legal action to which the board is a party, (C) in response to an official inquiry from a state or federal agency, (D) in response to a subpoena or summons enforceable by order of a court, or (E) when otherwise specifically required by law.

(5) Nothing in this subdivision shall impose a duty upon any licensee or nonlicensee owner to report to the board the occurrence of any events set forth in paragraph (7) of subdivision (a) or paragraph (2) of this subdivision either by or against any other nonlicensee owner.

(c) For purposes of this section, the following definitions apply:

(1) "Licensee" means a certified public accountant or public accountant in this state or a certified public accountant in good standing in another state.

(2) "Material participation" means an activity that is regular, continuous, and substantial.

(d) All firms with nonlicensee owners shall certify at the time of registration and renewal that the firm is in compliance with this section.

(e) The board shall adopt regulations to implement, interpret, or make specific this section.

BUSINESS AND PROFESSIONS CODE SECTIONS 5150-5158

5150. An accountancy corporation is a corporation which is registered with the California Board of Accountancy and has a currently effective certificate of registration from the board pursuant to the Moscone-Knox Professional Corporation Act, as contained in Part 4 (commencing with Section 13400) of Division 3 of Title 1 of the Corporations Code, and this article. Subject to all applicable statutes, rules and regulations, an accountancy corporation is entitled to practice accountancy. With respect to an accountancy corporation, the governmental agency referred to in the Moscone-Knox Professional Corporation Act is the California Board of Accountancy.

5151. An applicant for registration as an accountancy corporation shall supply to the board all necessary and pertinent documents and information requested by the board concerning the applicant's plan of operation. The board may provide forms of application. If the board finds that the corporation is duly organized and existing under the General Corporation Law or the foreign corporation is duly qualified for the transaction of intrastate business pursuant to the General Corporation Law, that, except as otherwise permitted under Section 5053 or 5079, each officer, director, shareholder, or employee who will render professional services is a licensed person as defined in the Moscone-Knox Professional Corporation Act, or a person licensed to render the same professional services in the jurisdiction or jurisdictions in which the person practices, and that from the application it appears that the affairs of the corporation will be conducted in compliance with law and the rules and regulations of the board, the board shall upon payment of the registration fee in the amount as it may determine, issue a certificate of registration. The applicant shall include with the application for each shareholder of the corporation licensed in a foreign country but not in this state or in any other state, territory, or possession of the United States, a certificate from the authority in the foreign country currently having final jurisdiction over the practice of accounting, which shall verify the shareholder' s admission to practice in the foreign country, the date thereof, and

the fact that the shareholder is currently in good standing as the equivalent of a certified public accountant or public accountant. If the certificate is not in English, there shall be included with the certificate a duly authenticated English translation thereof. The application shall be signed and verified by an officer of the corporation.

5152. Each accountancy corporation shall file with the board at the times the board may require a report containing information pertaining to qualification and compliance with the statutes, rules and regulations of the board as the board may determine. All reports shall be signed and verified by an officer of the corporation.

5152.1. Each accountancy corporation shall renew its permit to practice biennially and shall pay the renewal fee fixed by the board in accordance with Section 5134.

5154. Except as provided in Section 5079 of this code and in Section 13403 of the Corporations Code, each director, shareholder, and officer of an accountancy corporation shall be a licensed person as defined in the Moscone-Knox Professional Corporation Act, or a person licensed to render the same professional services in the jurisdiction or jurisdictions in which the person practices.

5155. The income of an accountancy corporation attributable to professional services rendered while a shareholder is a disqualified person (as defined in the Moscone-Knox Professional Corporation Act) shall not in any manner accrue to the benefit of such shareholder or his shares in the accountancy corporation.

5156. An accountancy corporation shall not do or fail to do any act the doing of which or the failure to do which would constitute unprofessional conduct under any statute, rule or regulation now or hereafter in effect. In the conduct of its practice, it shall observe and be bound by such statutes, rules and regulations to the same extent as a person holding a permit under Section 5070 of this

code. The board shall have the same powers of suspension, revocation and discipline against an accountancy corporation as are now or hereafter authorized by Section 5100 of this code, or by any other similar statute against individual licensees, provided, however, that proceedings against an accountancy corporation shall be conducted in accordance with Chapter 5 (commencing with Section 11500) of Part 1 of Division 3 of Title 2 of the Government Code, and the board shall have all the powers granted therein.

5157. The board may formulate and enforce rules and regulations to carry out the purposes and objectives of this article, including rules and regulations requiring (a) that the articles of incorporation or bylaws of an accountancy corporation shall include a provision whereby the capital stock of such corporation owned by a disqualified person (as defined in the Moscone-Knox Professional Corporation Act), or a deceased person, shall be sold to the corporation or to the remaining shareholders of such corporation within such time as such rules and regulations may provide, and (b) that an accountancy corporation as a condition of obtaining a certificate pursuant to the Moscone-Knox Professional Corporation Act and this article shall provide adequate security by insurance or otherwise for claims against it by its clients arising out of the rendering of professional services.

5158. Each office of an accountancy corporation engaged in the practice of public accountancy in this state shall be managed by a certified public accountant or public accountant.

State of California Department of Consumer Affairs

CALIFORNIA BOARD OF ACCOUNTANCY
2000 EVERGREEN STREET, SUITE 250
SACRAMENTO, CA 95815-3832
TELEPHONE: (916) 263-3680
FACSIMILE: (916) 263-3675
WEB ADDRESS: http://www.dca.ca.gov/cba

Attachment 6

PRACTICE PRIVILEGE TASK FORCE
MINUTES OF THE MEETING
March 17, 2005

Sheraton Delfina
530 W. Pico Blvd.
Santa Monica, CA 90405

CALL TO ORDER

Gail Hillebrand, Chair, called the meeting of the Practice Privilege Task Force to order at 8:36 a.m. and welcomed the participants. Ms. Hillebrand indicated that to ensure compliance with the Bagley-Keene Open Meeting Act, when a quorum of the Board is present at this meeting (eight members of the Board), Board members who are not serving on the Task Force must attend as observers only.

Present:
Gail Hillebrand, Chair
Sally Flowers
Thomas Iino
Hal Schultz
Renata Sos

Staff and Legal Counsel
Mary Crocker, Assistant Executive Officer
Patti Franz, Licensing Manager
Michael Granen, Deputy Attorney General
Greg Newington, Chief, Enforcement Program
LaVonne Powell, Legal Counsel
Michelle Santaga, Enforcement Analyst
Carol Sigmann, Executive Officer
Liza Walker, Regulation Analyst
Jeannie Werner, Deputy Attorney General
Aronna Wong, Legislation Coordinator

Other Participants
Michael Duffey, Ernst and Young LLP
Del Exeter, Society of California Accountants

Harish Khanna, Chair, Administrative Committee
Richard Robinson, Richard Robinson and Associates
Jeannie Tindel, California Society of Certified Public Accountants
Sarah Weber, Center for Public Interest Law

Board Members Observing
Richard Charney
Donald Driftmier
Cliff Johnson

I. Minutes of the January 20, 2005, Meeting

It was moved by Mr. Iino, seconded by Ms. Sos, and unanimously carried to approve the minutes of the January 20, 2005, meeting.

II. Consideration of Q&As Related to Practice Privilege.

Ms. Franz reported that questions were provided to staff at the request of the Chair at the meeting and developed by staff based on previous Task Force discussions. She explained that staff met to discuss the draft questions and prepare the answers provided to the Task Force (see Attachment 1).

Ms. Franz asked the Task Force members to review the questions and answers and provide comments. She explained that there were five various categories: General Inquiries, Requirements for Signing Attest Reports, Servicing of Clients, Safe Harbor Provisions, and Firm Licensure in California. Ms. Franz added that she would read each question under each category and provide an opportunity for the Task Force members to comment on the answer.

Mr. Schultz suggested the second sentence in the answer to Question 4 under General Inquiries be edited to read "*You will have the option of either submitting the Notification Form on-line or downloading the form from the Web site for submission through the mail.*" Mr. Duffey also suggested that the answer to Question 4 indicate that submission of faxed Notification Forms will also be acceptable for practice privilege. Ms. Wong explained that the regulations would need to be updated to include that information as well.

Ms. Sos suggested that the answer to Question 5 be more explicit in assisting an individual in locating the list of states that are currently deemed substantially equivalent by the Board. She also added that the second bullet of the practice privilege requirements should include the full process that an individual must complete to be deemed substantially equivalent by CredentialNet.

Ms. Hillebrand suggested that the second bullet of Question 5 be edited to read "*You must hold a valid, current license, certificate, or permit to practice public accountancy from another state and meet one of the following requirements.*"

Ms. Sos suggested the following edits to the answer to Question 10:

- "*You are required to reply to a Board request in a timely manner [cross reference to Section 5096(e)(5)], which may extend beyond the expiration of your practice privilege.*"
- Include the wording "*The Notification Form must be completed in its entirety.*"

Ms. Wong added that if the individual has a disqualifying condition, submission of additional documentation will be required prior to commencing practice in California under the practice privilege.

During the review of Question 11, Ms. Powell asked Ms. Franz whether there is a consequence if a licensee allows his or her license to lapse. Ms. Franz responded that a license that is not renewed for five consecutive years is cancelled. She explained the reissuance process that an individual must comply with to obtain a license to practice public accountancy in California after the previous license has cancelled. Ms. Powell indicated that she thought the answer to Question 11 should indicate that there is a consequence if a licensee allows the license to lapse.

Ms. Sos suggested that the individual should contact the Board before making the decision regarding whether to allow the license to lapse and practice under a practice privilege. Ms. Franz suggested the answer to Question 11 could direct the licensee to review the information related to the consequences, such as the Licensee Handbook, on the Board's Web site. She indicated that if the individual were unable to determine the consequences from the Handbook, he or she could contact Board staff. Ms. Sos agreed that Ms. Franz's idea was better than trying to spell out all of the possible scenarios in the Q&As. Ms. Franz suggested that Question 11 be edited to read "*I am licensed in California and in Texas. My principal place of business is not in California. Can I practice public accountancy in California under practice privilege if my California license is inactive, delinquent, or cancelled?*" After discussion, Ms. Hillebrand agreed that the wording proposed by Ms. Franz would be clearer.

Mr. Iino suggested that the word "*other*" be removed from the answer to Question 11. Ms. Hillebrand agreed, and the last sentence of the answer was edited to read "*and meet all requirements to obtain and maintain California practice privilege.*"

Ms. Hillebrand suggested that Question 2 under Requirements for Signing Attest Reports include the same language as Question 10 under General Inquiries.

After Ms. Franz read Question 1 under Servicing of Clients, Mr. Schultz suggested that "*Through the mail*" should be struck from Question 1 under Servicing of Clients to alleviate confusion that the use of the Internet, or some other sort of manner of not physically entering California, would not apply.

Mr. Granen stated that he did not have an issue with the answer to Question 1 under Servicing of Clients, except the statement regarding the firm registration. He commented that if an individual is licensed and comes into California to do work – whether an inventory observation or a tax return, and that person signs on behalf of the firm or the inventory is done and incorporated into an audit issued under the firm name – the firm should not be required to register. He stated that he thought it would be going too far to say the firm itself would have to be registered if the only way the firm sets foot in California is through the individual holding a practice privilege.

Mr. Newington stated that staff struggled with these issues. The intent was to establish a bright-line test related to practice privilege. He explained that, as staff went through the various scenarios, the test was if the individual physically comes into California to perform the activities in subdivisions (a) – (f) of Section 5051 or services California clients from outside the state, this is practicing public accountancy in California.

Mr. Newington added that as staff considered these scenarios, staff noted that the firm was signing the engagement or the tax return. He asked if a firm from another state sends in personnel who are not CPAs, which is allowed, who would the Board hold accountable for the work other than the firm? He summed it up by stating that if a firm practices public accountancy through its agent – either a licensed or unlicensed individual – physically entering California or through servicing California clients, this is practicing public accountancy as defined in Section 5051 and the firm needs to be registered. He added that he understood that the answers would be controversial and may make it difficult for small firms to practice in California due to the partner or shareholder licensure requirement for firm registration.

Ms. Hillebrand stated that the reason for the discussion is to remind people that the firm requirements will still apply regardless of what the individual is doing under the practice privilege. Mr. Newington agreed, and stated that staff will receive calls regarding the requirements for both individuals and firms and need clear guidance in order to be prepared to respond to inquiries.

Mr. Granen indicated that if firms will be required to register in California, it will not be economical for small firms to perform audits in California. For that reason, he stated he thought there was good reason to take another approach. He expressed the view that if a firm is not coming into the state other than through an agent with a valid practice privilege that the firm should not be required to register. He explained that that approach would put small firms in the same position as the large firms that are already registered in California.

Ms. Hillebrand stated that she disagreed with this interpretation of the current law because the law does not include a practice privilege equivalent for firms. She stated that in her opinion the answer to the question is accurate based upon the current statute.

After discussion, Ms. Hillebrand indicated that the policy issue before the Task Force relates to the fact that the practice privilege statute does not create a privilege for firms. This means an individual who holds a practice privilege cannot come into California on behalf of an out-of-state firm. Further, for an out-of-state firm to register in California a partner or shareholder needs to obtain a California license. Mr. Iino commented that if one works for a firm, he cannot conceive of signing as an individual. He explained that the signatures are almost always entirely signed in the name of the firm. Mr. Newington indicated he believed this was a significant issue.

Ms. Hillebrand asked Mr. Newington whether he had any indication of how many firms currently practicing in California under the temporary provision do not have a California licensee as a partner or shareholder. Mr. Newington responded that he was sure some firms are practicing under the temporary provision, but that the volume was hard to quantify. He stated that based upon the telephone calls he has received from out-of-state practitioners regarding California practice privilege, the tax issue is of much more concern than the audit inventory issue.

Ms. Sos inquired if a practice privilege holder comes in and signs an attest report on behalf of the firm, is there a concern regarding the Board's jurisdiction if the firm is not registered? Mr. Granen indicated that if the firm is not registered in California, there is no registration to revoke or discipline. Mr. Newington stated that he believed the Board does have jurisdiction over the firm and its agents, either licensed or unlicensed. As with other instances of unlicensed practice, the Board could issue a citation or pursue a misdemeanor violation.

Participants then discussed potential solutions to the problem they had identified. Mr. Newington suggested that a potential fix would be to include a practice privilege for firms. He explained that if that solution were provided, the issues being discussed by the Task Force would be addressed. Mr. Granen suggested the Board could adopt the policy that if the firm's practice in California is limited only to the activities of the practice privilege holder who is coming into the state, then that would be acceptable. Ms. Hillebrand invited discussion on Mr. Granen's proposal indicating if the firm's only activities in California are undertaken by a person holding a practice privilege, then the firm would not be required to register. Ms. Crocker stated that this approach would constrain a firm's ability to send a nonlicensee to California. This should really be a business decision by the firm and not a decision based on regulatory requirements. Ms. Hillebrand suggested that any proposal which might allow firms to register with a practice privilege holder would require further investigation. Ms. Sos indicated she did not believe it was appropriate to allow firms to register with only practice privilege holders and no California licensee. The practice privilege concept was developed only for individuals so that qualified out-of-state CPAs can practice in California temporarily.

After further discussion, Ms. Hillebrand identified the following issues for future Task Force consideration: 1) If an agent of a firm is coming into California to practice public accountancy, should that firm be required to register? 2) Should a firm be able to register in California with a practice privilege holder in lieu of a California licensee as a

partner or shareholder? 3) Would such a firm have the same limitations and restrictions as an individual practice privilege holder? She asked staff to look at the identified issues and provide the pros and cons of pursuing such a statutory change. Ms. Hillebrand explained she wanted staff to explore whether it is possible to create a limited form of firm registration that would be available to firms that have a practice privilege holder, and the potential negative consequences of doing so. This limited form of firm registration would be designed to permit the firm to practice public accountancy in California in a manner similar to the practice privilege holders.

Ms. Powell asked the Task Force to consider whether there would be anything that would be taken away except for the individual's practice privilege in the event there was any disciplinary action against the firm. Mr. Granen responded that he thought it would be easy to craft a limited firm practice privilege that could be taken away in those instances.

Ms. Franz asked whether the firms as well as the individual practice privilege holders would show up on the Web site. Ms. Hillebrand responded that this also needed to be explored and to make sure that any limited firm practice privilege which might be considered would not cause more of a problem then it solved. Ms. Hillebrand further stated she wanted this to be carefully thought out before developing any recommendation about going before the Legislature again.

Ms. Crocker asked the Task Force to identify which problem they were attempting to address:

- Firms would be sending staff to California and, by doing so, create a situation in which firms that are not registered in California would be practicing public accounting unlawfully; or
- Firms would be sending unlicensed individuals or individuals who do not acknowledge they are CPAs to avoid obtaining practice privileges.

Ms. Crocker also requested clarification from the Task Force whether staff should proceed with the current development of the database and procedure development for implementation of practice privilege although a major policy issue was identified at the meeting. She explained that the database for practice privilege is not currently being built to include anything related to firm registration and asked whether staff should proceed with the current development. She explained that the time frames are tight as the effective date is January 1, 2006. Ms. Hillebrand responded that she did not want staff to pause in the implementation process while this policy issue is being researched.

Ms. Hillebrand stated that she believed there is a fair amount of work that needed to be completed by staff in researching the policy issues identified. Ms. Sos suggested that a sub-Task Force, including herself and Ms. Hillebrand, would work with staff on the policy issues related to the firm registration to determine whether there is a solution that creates fewer problems than it solves.

The Task Force then returned to consideration of the Q&As as a whole.

Mr. Schultz commented that the answer to Question 6 under Servicing of Clients was incorrect as it refers to the engagement partner, who may not be doing the inventory observation in California. After discussion, it was suggested by Ms. Hillebrand that the answer be edited to read "*Yes, if you or any other person physically enters California to practice public accountancy, that person is required to obtain a California practice privilege or a California CPA license.*"

It was moved by Ms. Sos, seconded by Ms. Flowers, and unanimously carried to approve the Q&As related to Practice Privilege with the changes noted above. Ms. Sos thanked staff for their hard work in developing the Q&As for the Practice Privilege Task Force.

III. Consideration of What Practice Privilege Information Should be Available on the Board's Web Site.

Ms. Franz reported on the items that staff were proposing to be placed on the Board's Web site specifically for practice privilege holders. She stated each of the bullets provide descriptions of those items, including proposed definitions (Attachment 2).

She identified one change that she would like the Task Force to consider regarding the Practice Privilege Status for the Web site. She explained that within the agenda item there is one status, "Clear." Her suggestion was to include "Administrative Suspension" and "Revoked" as statuses on the Web site, instead of under "Disciplinary Actions." She added that under "Disciplinary Actions" there would be an indicator either "Y" or "N." Ms. Hillebrand stated that it would be helpful to have "Administrative Suspension" and "Revoked" also as a status along with "Clear." Ms. Franz also asked the Task Force to consider if the practice privilege status was reflected as Administrative Suspension, should the "Y" indicator be reflected under "Disciplinary Actions." Ms. Powell responded that the "Disciplinary Actions" field should be populated with the "Y" indicator if the practice privilege status is "Administrative Suspension."

Ms. Sos also stated that she believed the Administrative Suspension was a gray area and expressed concern regarding whether an individual who clears up the Administrative Suspension in a timely manner should have the "Y" indicator placed in the Disciplinary Action field.

Ms. Werner suggested changing the title of the field "Disciplinary Actions" to "*Enforcement actions other than citations.*" Ms. Franz suggested that there be a definition that indicates what enforcement actions include, and another definition that indicates what enforcement actions do not include. Ms. Hillebrand agreed that would be helpful.

State of California
Department of Consumer Affairs

Attachment 1

California Board of Accountanc
2000 Evergreen Street, Suite 25
Sacramento, CA 95815-383

Memorandum

Practice Privilege TF Agenda Item II.
March 17, 2005

Board Agenda Item VIII.F.3.
March 18, 2005

To : Practice Privilege Task Force Members
Board Members

Date : March 8, 2005

Telephone : (916) 561-1740
Facsimile : (916) 263-3676
E-mail : pfranz@cba.ca.gov

From : Patti L. Franz
Licensing Manager

Subject : Q&As Related to California Practice Privilege

Provided for consideration and action by the Task Force and Board are the following Q&As developed by staff related to the practice privilege provisions. It is anticipated the following Q&As will be placed on the Board's Web site in accordance with the Communication and Outreach plan provided for consideration at this Task Force meeting.

Introductory Narrative for Q&As

Legislation was signed into law in 2004 providing the California Board of Accountancy (Board) with the California practice privilege provision. The practice privilege provisions will go into effect on January 1, 2006. The practice privilege will allow cross-border practice under which a qualified out-of-state Certified Public Accountant (CPA) may temporarily practice public accountancy in California without having to obtain a California CPA license.

To qualify for a practice privilege, an out-of-state CPA will be required to notify the Board of the intent to practice public accountancy in California, swear under penalty of perjury that the requirements for a California practice privilege have been met, and agree to follow California law and be subject to the full force of the Board's enforcement and disciplinary powers.

The *Notification and Agreement to Conditions for the Privilege to Practice Public Accounting in California Pursuant to California Business and Professions Code Section 5096 and Title 16, Division 1, Article 4 of the California Code of Regulations Form* (Notification Form) and instructions will be available on the Board's Web site on our Forms/Publications Page for on-line submission and for downloading purposes. Once available, you may also contact the Board's Practice Privilege Unit at *pracprivinfo@cba.ca.gov* or telephone (916) 561-XXXX to request that a form be mailed to you.

The practice privilege expires one year from the date of on-line submission or mailing of the hardcopy Notification Form. The fee required for a California practice privilege is $100 and must be received by the Board within 30 days of Notification Form submission.

General Inquiries

1. *Q: When will the California practice privilege provision go into effect?*

   A: The California practice privilege provision will become effective on January 1, 2006.

2. *Q: Where can I find the statutes and regulations regarding practice privilege?*

   A: Sections 5096 through 5096.11 of the California Business and Professions Code (Accountancy Act) and Sections 26 through 35.1 of Title 16 of the California Code of Regulations (Accountancy Regulations) will be available on the Board's Web site at *www.dca.ca.gov/cba* or from the Practice Privilege Unit at (916) 561-XXXX.

3. *Q: Where can I locate the practice privilege Notification Form?*

   A: The practice privilege Notification Form will be available on the Board's Web site at *www.dca.ca.gov/cba* on our Forms/Publications Page or from the Practice Privilege Unit at *pracprivinfo@cba.ca.gov* or from the Practice Privilege Unit at telephone (916) 561-XXXX.

4. *Q: How can I submit the Notification Form?*

   A: The practice privilege Notification Form will be available on the Board's Web site at *www.dca.ca.gov/cba* on the Forms/Publications Page. You will either have the option of submitting the Notification Form on-line or downloading the form from the Web site for submission through the mail.

   Once the form is submitted on-line or mailed, the practice privilege expires one year from the submission date. The fee required for a California practice privilege is $100 and must be received by the Board within 30 days of Notification Form submission.

5. ***Q: What requirements must I fulfill for a practice privilege in California?***

A: To be eligible for a California practice privilege:

1. Your principal place of business cannot be located in California.

2. You must hold a valid, current license, certificate, or permit from another state and meet one of the following requirements:

- Hold a current, valid license, certificate, or permit from a state determined by the Board to have education, examination, and experience requirements for licensure substantially equivalent to the requirements in Section 5093 of the California Accountancy Act (see Appendix 1 of the Notification Form). **OR**;
- Possess education, examination, and experience qualifications that have been determined by the Board to be substantially equivalent to the qualifications under Section 5093 of the California Accountancy Act. **OR**;
- Have continually practiced public accountancy as a CPA under a current, valid license issued by any state for four of the last ten years.

3. If you have any of the disqualifying conditions identified on the practice privilege Notification Form, you may not practice public accountancy in California until you receive Board approval.

6. ***Q: I am a CPA but am not licensed in a state that is deemed substantially equivalent in Appendix 1 of the Notification Form. What options do I have to qualify for a California practice privilege?***

A:

1. Have continually practiced public accountancy as a CPA under a current, valid license issued by any state for four of the last ten years. **OR**;

2. Submit documents reflecting successful passage of the CPA examination, college transcripts and documents reflecting completion of experience to the National Association of State Boards of Accountancy's (NASBA) CredentialNet. CredentialNet will evaluate your licensure information and determine equivalency. Information regarding CredentialNet can be found on NASBA's Web site at *www.nasba.org*.

   If deemed substantially equivalent, a file number will be given to you. At the time you submit your Notification Form to the Board, you will be required to provide your NASBA CredentialNet file number.

7. *Q: I am an out-of-state CPA who is applying for licensure in California. Do I have practice rights in California as my application is being processed?*

   A: No, you do not have practice rights as a CPA in California.

   In order to have practice rights while the Board is processing your California licensure application, you will be required to submit the practice privilege Notification Form as well as the $100 notification fee. The notification fee must be received by the Board within 30 days of your Notification Form submission. Your practice privilege will be terminated at the time your California CPA license is issued by the Board.

8. *Q: As an out-of-state CPA, is there a limit to the number of times I can submit the practice privilege Notification Form as opposed to applying for California licensure?*

   A: The statute and regulations pertaining to practice privilege do not identify a limitation to the number of times you can submit the Notification Form for a practice privilege.

9. *Q: Can I open a California office and practice full or part-time there under a practice privilege?*

   A: No. Pursuant to Section 5096(e)(3) of the California Accountancy Act, a practice privilege holder cannot provide public accountancy services in California from any office located in this state, except as an employee of a firm registered in this state or in the client's office.

10. *Q: What documentation must I provide for a California practice privilege?*

    A: You are not required to submit documentation with the practice privilege Notification Form. However, the Board has the authority to request documentation from you and verify any of the information you provide on the Notification Form.

11. *Q: I am licensed in California and in Texas. My principal place of business is not in California. Can I practice public accountancy in California under practice privilege and allow my California license to lapse?*

    A: Yes, you can allow your California CPA license to lapse and practice under the practice privilege as long as you have a valid, current CPA license in another state and meet all other requirements to obtain a California practice privilege.

12. ***Q: I am a California CPA and prepare tax returns for a few clients in other states. Do other states require a practice privilege in order to continue to serve these clients?***

A: The requirements to practice public accountancy vary from state to state. It is your responsibility to comply with the laws and requirements of any jurisdiction in which you practice. Therefore, it is suggested you contact the relevant state board(s) to determine what is required. Unauthorized practice in another state can be cause for discipline against your California license.

Requirements for Signing Attest Reports

1. ***Q: What experience must I fulfill before I sign an attest report under a California practice privilege?***

A: You may not sign an attest report unless you have completed 500 hours of experience in attest services as described in Section 5095 of the California Accountancy Act. Qualifying experience is that which has enabled you to demonstrate an understanding of the requirements of planning and conducting an audit with minimum supervision that results in opinions on full disclosure financial statements.

2. ***Q: What documentation must I provide to be able to sign an attest report in California under the practice privilege?***

A: You are not required to submit any documentation with the practice privilege Notification Form. However, the Board has the authority to request documentation from you and verify any of the information you have submitted on the Notification Form, including whether you have fulfilled the attest experience requirement to sign an attest report in California prior to the issuance of the practice privilege.

Servicing of Clients

1. ***Q: I'm a CPA in another state and do not plan to be in California. Through the mail, I do only one tax return for a California client. Do I need a California practice privilege?***

A: Yes, in order to provide public accounting services to clients who reside in California you will be required to obtain a California practice privilege or obtain a California CPA license. Preparing tax returns as a CPA is a service that falls within the definition of the practice of public accountancy contained in Section 5051 of the California Accountancy Act.

If tax returns are prepared in the name of a firm, the firm would also need to be registered in California. You can visit the Board's Web site at *www.dca.ca.gov/cba* to review the firm registration requirements and obtain the application.

2. ***Q: I'm a CPA in another state. One of my clients retired and moved to California. Do I need a practice privilege to continue to prepare that client's tax return?***

   A: Yes, in order to provide public accounting services to clients who reside in California you will be required to obtain a California practice privilege or obtain a California CPA license. Preparing tax returns as a CPA is a service that falls within the definition of the practice of public accountancy contained in Section 5051 of the California Accountancy Act.

   If tax returns are prepared in the name of a firm, the firm would also need to be registered in California. You can visit the Board's Web site at *www.dca.ca.gov/cba* to review the firm registration requirements and obtain the application.

3. ***Q: I will be performing work in California on an audit engagement on a contract basis for another CPA who is a sole proprietor and is not licensed in California. Who will need to be licensed or obtain a practice privilege?***

   A: The non-California CPA responsible for the audit would need to obtain a California practice privilege or California CPA license. If you as the contracted individual hold out (identify yourself) as a CPA while performing work on the audit, you also would need to obtain a California practice privilege or California CPA license.

4. ***Q: I am a Utah CPA who prepares state tax returns filed with the California Franchise Tax Board for my Utah resident clients. Do I need a practice privilege after December 31, 2005?***

   A: No. However, you would need to obtain a California practice privilege or obtain a California CPA license to practice public accountancy as defined in Section 5051 of the California Accountancy Act if you intend to service clients who reside in California.

5. ***Q: If I need to conduct part of my audit work in California for a client principally based in Florida, do I need to secure a practice privilege under the new requirements?***

   A: Yes, in order to physically enter California to practice public accountancy as defined in Section 5051 of the California Accountancy Act you need to obtain a California practice privilege or obtain a California CPA license.

   If the audit report will be issued under the name of the firm, the firm would need to be registered in California. You can visit the Board's Web site at *www.dca.ca.gov/cba* to review the firm registration requirements and obtain the application.

6. ***Q: My client's primary business operation is located in California. However, their administrative office is located in Washington. I have been engaged to conduct an audit. All the work will be done in Washington, except for the inventory observation. Do I, as the engagement partner, need to obtain practice privilege?***

A: Yes, if you physically enter California to practice public accountancy as defined in Section 5051 of the California Accountancy Act you will be required to obtain a California practice privilege or California CPA license. Audit services, including inventory observation, fall within the definition of the practice of public accountancy.

The firm would also need to be registered in California. You can visit the Board's Web site at *www.dca.ca.gov/cba* to review the firm registration requirements and obtain the application.

7. ***Q: I am an out-of-state CPA who performs peer reviews for California accountancy firms. Would I be required to obtain a California practice privilege?***

A: No, you would not be required to obtain a California practice privilege. Performing a peer review for a California accountancy firm is not a service that falls within the definition of the practice of public accountancy contained in Section 5051 of the California Accountancy Act.

Safe Harbor Provision

1. ***Q: When am I required to notify the Board that I'm practicing public accountancy in California under the practice privilege?***

A: Notice is required on or before beginning practice. However, there will be no penalty if the notice is given within five business days of commencing practice. The safe-harbor provision for this short delay in the notice is only effective through December 31, 2007. Because the notification requirements for practice privilege are new, the Board will permit a five-business day safe-harbor period for notification for the first two years. This will allow time for licensees to become familiar with the practice privilege requirements.

If the Notification Form is submitted after practice began in California, even if it is submitted within the five-day safe-harbor period, you will be required to provide a reason why the notice was not submitted prior to the date practice began in California.

Firm Licensure in California

1. *Q: I work for a CPA firm that is licensed in the State of Maryland. We have an opportunity to do audit work in California. We would be sending one CPA to California to perform the audit work for one week. The audit report will be issued in Maryland under the firm name. Does the CPA who is coming to California need a practice privilege? What type of license does the firm need?*

   A: Yes, notice is required to commence practice of public accountancy in California. In order to practice public accountancy as defined in Section 5051 of the Accountancy Act in California or service clients who reside in California the non-California CPA who is performing the audit work in California will be required to obtain California practice privilege or obtain a California CPA license.

   In addition, the firm would need to be registered with the California Board of Accountancy. You can visit the Board's Web site at *www.dca.ca.gov/cba* to review the firm registration requirements and obtain the application.

State of California Department of Consumer Affairs

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Attachment 7

Board Agenda Item VIII.G. 1
July 22, 2005

PRACTICE PRIVILEGE TASK FORCE
MINUTES OF THE MEETING
May 19, 2005

DRAFT

The Westin Horton Plaza
910 Broadway Circle
San Diego, CA 92101

CALL TO ORDER

Gail Hillebrand, Chair, called the meeting of the Practice Privilege Task Force to order at 9:00 a.m. and welcomed the participants. Ms. Hillebrand indicated that to ensure compliance with the Bagley-Keene Open Meeting Act, when a quorum of the Board is present at this meeting (eight members of the Board), Board members who are not serving on the Task Force must attend as observers only.

Present:
Gail Hillebrand, Chair
Thomas Iino
Hal Schultz
Renata Sos

Staff and Legal Counsel
Mary Crocker, Assistant Executive Officer
Patti Franz, Licensing Manager
Michael Granen, Deputy Attorney General
Greg Newington, Chief, Enforcement Program
LaVonne Powell, Legal Counsel
Carol Sigmann, Executive Officer
Liza Walker, Regulation Analyst
Jeannie Werner, Deputy Attorney General
Aronna Wong, Legislation Coordinator

Other Participants
Bruce Bialosky, CPA
Julie D'Angelo-Fellmeth, Center for Public Interest Law
Michael Duffey, Ernst and Young LLP
Bill Gage, Chief Consultant, Senate Committee on Business, Professions & Economic Development
Kenneth Hansen, Chief Operations Officer, KPMG LLP

Harish Khanna, Chair, Administrative Committee
Richard Robinson, Richard Robinson and Associates
Jeannie Tindel, California Society of Certified Public Accountants

Board Members Observing
Richard Charney
Donald Driftmier
Olga Martinez

I. Minutes of the March 17, 2005, Meeting

It was moved by Mr. Schultz, seconded by Ms. Sos, and unanimously carried to approve the minutes of the March 17, 2005, meeting.

II. Adoption of Appendix 1 to the Practice Privilege Notification Form.

Ms. Franz reported that at the September 2004 meeting the Board adopted the Task Force's recommendation that the Board accept the National Association of State Boards of Accountancy's (NASBA's) list of substantially equivalent states, subject to continuous monitoring by the Board, in lieu of the Board reviewing each individual state's requirements and developing its own list. She explained that Attachment 3 to her May 10, 2005, memo provided the current list of those states for consideration and action by the Task Force (see Attachment 1). Ms. Franz indicated that it is envisioned that the list of substantially equivalent states will become part of the instructions for the Notification Form.

Ms. Sos stated that she believed the second sentence on the list of substantially equivalent states is unnecessary. She noted that when she read the sentence, she did not believe it was quite accurate, and given that this will accompany the instructions, it is not necessary. She added that she believed deleting this sentence would improve the clarity of the narrative provided with the list.

After discussion, it was moved by Mr. Schultz, seconded by Ms. Sos, and unanimously carried to recommend Board approval of Appendix 1 with the change suggested by Ms. Sos.

Ms. Franz also reported that there was one outstanding issue related to Appendix 1. She explained that, as NASBA adds or deletes states from the list, some mechanism may be needed to enable the Board to add or delete states from Appendix 1 without action at a Board meeting. She indicated that staff suggest that the Task Force consider delegating to either the Executive Officer or the leadership of the Board the authority to act upon changes NASBA makes to its list rather than waiting for the next Board meeting.

Ms. Hillebrand stated that she would be inclined to delegate the authority to the Executive Officer. Ms. Sigmann explained that there would be a report to the Board at the meeting subsequent to any action taken by the Executive Officer.

After discussion, it was moved by Ms. Sos, seconded by Mr. Schultz, and unanimously carried to delegate the authority to the Executive Officer to maintain Appendix 1 as NASBA makes changes to its list of substantially equivalent states.

Ms. Hillebrand reported that at the last meeting, the Task Force had recommended that the Board suggest to NASBA that it undertake the job of making available to the profession information regarding practice privilege requirements in various states. She noted that staff have sent a letter communicating this request.

III. Consideration of an Approach to Address Issuance of Reports Under the Name of Non-Registered Firms.

Ms. Hillebrand introduced this agenda item by noting that at the last Task Force meeting there was discussion of various concerns related to the issuance of reports under the name of a non-registered firm and how that could best be addressed. This issue arose during the discussion of the "Q&As" related to practice privilege. One of the questions staff anticipated would be asked was "If I am an individual holding a practice privilege, can I sign a tax return on behalf of my firm?" It was noted that, under current law, after January 1, 2006, the firm would have to be registered in California, before that question could be answered affirmatively. Ms. Hillebrand added that after the discussion at the last Task Force meeting, she and Ms. Sos were tasked with responsibility for working with staff and legal counsel to explore how to address this issue.

Ms. Hillebrand then asked Ms. Crocker to describe the proposal that was developed. Ms. Crocker reported that after discussing the issue, it was concluded that the best approach would be to create a narrow exception from the requirements for firm registration in the area of tax prepartion. In pursuing a way to craft that exception, the working group first identified areas where no exception would be possible. It was determined that anytime an individual physically enters California to practice public accountancy as an agent of a firm, that individual must be affiliated with a California-registered firm. Also, any time a firm performs financial statement work there is sufficient consumer risk so the firm must be registered with the Board. Ms. Crocker explained that after further discussion, the working group concluded that an exemption from firm registration would only be reasonable in those instances in which the practitioner is preparing individual tax returns, does not physically enter California, does not solicit any California clients, and does not assert or imply that the individual or firm is licensed or registered to practice public accountancy in California. Ms. Crocker added that this individual would be exempt from licensure and practice privilege requirements as well. She noted that draft statutory language provided is in the materials for this agenda item (Attachment 2).

Ms. Hillebrand added that the working group was asked to develop a way in which someone could hold the practice privilege and sign a tax return on behalf of his or her firm without the firm being registered in California. The working group found that any solution it considered using this approach appeared to cause more problems than it solved, and it seemed more appropriate to carve out a very narrowly defined activity that would not require a practice privilege. She added that it is for this reason that the exemption is fairly narrow and the person would be required to meet all of the conditions described by Ms. Crocker.

Ms. Hillebrand then asked for comments or questions from Task Force members. Mr. Schultz stated that he believed that this approach is well thought out because an individual may establish a relationship with a CPA outside of California and should be able to continue that relationship. He stated that he did not believe that there was any consumer harm in allowing for this narrow exception. He then inquired about a situation in which an out-of-state firm sends someone to California to perform an inventory observation. Ms. Crocker indicated that she believed that since this is attest work it would not fit within the criteria for the exception.

Mr. Iino observed that the relevant terms in this proposal were "individual tax returns" and "physical entry into California." He asked about whether it would be permissible to complete partnership, corporate, sales tax, or property tax returns under the narrow exception. Ms. Crocker responded that the language as provided would not permit partnership or corporate tax returns.

Ms. Wong indicated that the working group chose this approach because individual tax returns seemed to be the area where the Board received the most comments from individuals regarding possible difficulty. Mr. Granen explained that the language provided solves a problem that has been raised at the national level. Ms. Hillebrand added that whatever place the Board chooses to draw a line, there will be close cases on both sides.

Ms. Hillebrand then invited any public comments regarding the proposal. Mr. Bruce Bialosky, CPA, provided oral comments regarding the proposal and provided a written summary of his remarks (Attachment 3). He explained that he was greatly concerned about the potential the problems practice privilege requirements could create and requested that the preparation of individual tax returns be exempted. He noted that many CPAs prepare tax returns for their client's children or prepare multi-state tax returns. Also, many consumers maintain a long-term relationship with the CPA from the state where they lived prior to moving to California. He noted that California rules are held in high regard in other states, and he was concerned that the practice privilege laws could result in reciprocal requirements in other states.

Mr. Schultz asked Mr. Bialosky whether he would like to see anything beyond proposed Section 5054. Mr. Bialosky responded that the proposed statute addressed his concerns with California practice privilege. Mr. Schultz observed that there appeared to be general agreement regarding the concept embodied in the proposed Section 5054.

The Task Force then considered whether there should be modifications to the language of proposed Section 5054 to specify particular types of tax returns or to specify a level of complexity. Mr. Newington noted that there are many other kinds of tax returns besides individual income tax returns – for example sales tax, property tax, and estate tax returns. Mr. Iino indicated that tax returns prepared for individual persons could still be very complex. Ms. Hillebrand indicated that the only reason the exemption was acceptable to her was that it applied to individual tax returns but did not permit the preparation of tax returns for corporations or other business entities. She suggested that the language could be revised to indicate "personal individual income tax returns." She added that she did not know of a way to address complexity. Ms. Sos suggested that rather than trying to address the type and complexity of the tax return in the statute, perhaps subdivision (b) could be revised to permit the Board to address these issues in regulations.

Ms. Hillebrand then summarized the discussion by noting that there appeared to be consensus regarding the general concept. She added that the remaining issues are whether the language should be revised to restrict it to personal, individual income tax returns and whether subdivision (b) should be revised to permit the nature and complexity of the tax return to be addressed in regulations. Ms. Hillebrand suggested a break so that draft language could be prepared for further discussion by the Task Force.

After the break, Ms. Hillebrand noted that language had been drafted related to estate tax returns. At Ms. Hillebrand's request, Mr. Granen read the following language to the Task Force:

> *Notwithstanding any other provision of this chapter, an individual or firm holding a valid and current license, certificate, or permit to practice public accountancy from another state may prepare tax returns for natural persons who are California residents and the estate tax return for the estate of a natural person who was a client at the time of the client's death without obtaining a permit to practice public accountancy issued by the Board under this chapter or a practice privilege pursuant to Article 5.1 of this chapter provided that the individual or firm does not physically enter California to practice public accountancy pursuant to Section 5051, does not solicit California clients, and does not assert or imply that the individual or firm is licensed or registered to practice public accountancy in California.*

The Task Force decided to delay action on this amendment until the other remaining issues had been addressed.

Mr. Iino suggested deleting the word "individual." Ms. Werner noted that the word "individual" could be interpreted as a discrete or single tax return which is the not the intention. Ms. Wong added that she believed that with the use of the term "natural person" the word "individual" was not necessary. It was the consensus of the Task Force to delete the word "individual."

Ms. Hillebrand raised the question of whether the proposed statute should be restricted to income tax returns or whether all types of tax returns should be included. She explained that this issue was raised by practitioners who would like to continue preparing income tax returns for clients who have moved to California or have family members in California. She stated she was concerned that permitting other kinds of returns may suggest a deeper connection with the client in California. She asked the licensee members of the Task Force to indicate the types of returns that would not be permitted if the word "income" was added. Mr. Iino explained that if the word "income" was added to the language, gift, property, and sales tax returns would not be permitted. After discussion, it was the consensus of the Task Force to not add the word "income."

Ms. Hillebrand noted that the concept of practice privilege was introduced as a way of ensuring that the Board knows who is serving California clients. She believed that, when proposing an exception, it was the Board's responsibility to keep that exception as narrow as possible while still making it workable.

After further discussion, it was moved by Mr. Iino, seconded by Ms. Sos, and unanimously carried to recommend Board approval of proposed Section 5054 with the deletion of the word "individual" and the addition of the estate tax return language suggested by Mr. Granen.

Ms. Hillebrand thanked the Task Force members for all of their work to date and noted that the Q&As may need updating to reflect the policy decisions that were made this meeting. However, these changes were premature until the statutory language was enacted. Ms. Sigmann stated that staff will make every effort to pursue legislation, and it is possible that the statute will be in place by January 1, 2006, provided there is no opposition. Ms. Hillebrand indicated that the Task Force would reconvene in September to update the Q&As, and by that time the Board would know if the statute would be in place on January 1, 2006.

IV. Comments from Members of the Public.

Members of the public provided comments during the course of the meeting.

There being no further business, the meeting was adjourned at 10:55 a.m.

State of California
Department of Consumer Affairs

Attachment 2

California Board of Accountancy
2000 Evergreen Street, Suite 250
Sacramento, CA 95815-3832

Memorandum

Practice Privilege TF Agenda Item III
May 19, 2005

Board Agenda Item VIII.F.4
May 20, 2005

To : Practice Privilege Task Force Members
Board Members

Date : May 4, 2005

Telephone : (916) 561-1788
Facsimile : (916) 263-3674
E-mail : awong@cba.ca.gov

From : Aronna Wong - Aronna
Legislation/Regulations Coordinator

Subject : Consideration of an Approach to Address Issuance of Reports Under the Name of Non-Registered Firms

At the last Practice Privilege Task Force meeting, it was noted that most financial statement reports issued by licensees and most tax returns prepared by licensees are signed with the firm name. It was also noted that while the practice privilege provisions provide for cross-border practice by individuals, there are no comparable provisions for firms. Consequently, under current law, for a firm to practice public accountancy in California which would include performing activities such as reporting on financial statements or preparing tax returns for individual taxpayers or California companies, the firm would need to register with the Board.

This does not pose a problem for larger firms because most larger firms are already registered and have a presence in California. However, it can be challenging for smaller firms since these firm would have to meet all of California's ongoing registration requirements including the requirement that a partner or shareholder hold a California license.

After discussion, the Task Force concluded the issue needed further consideration and a working group consisting of Renata Sos and Gail Hillebrand was appointed to work with staff to develop a proposal for consideration at the May 2005 meetings of the Task Force and the Board.

After evaluating the possibility of a practice privilege for firms and an expedited procedure for qualifying for firm registration, the working group concluded that because of the numerous statutory requirements that tie to registered firms, neither of these two options was practical. During the discussion it was also noted that the greatest concern in this area was expressed by tax practitioners.

After discussion, it was concluded the most workable solution would be to carve out a narrow exception from the firm registration requirement. The working group began crafting its proposal by first identifying areas where no exception was possible. It was determined that any time an individual physically enters California to practice public accountancy as an agent of a firm, that individual must be affiliated with a California-registered firm. It was also determined that any time a firm performs financial statement work, there is sufficient consumer risk so that the firm must be registered with the Board.

After further deliberation, the working group concluded that an exception from the firm registration requirement would be reasonable only in those instances in which the practitioner is preparing individual tax returns, does not physically enter California, does not solicit any California clients, and does not assert or imply that the individual or firm is licensed or registered to practice public accountancy in California. It was further concluded that, for consistency, it would also be appropriate to provide an exception from the individual licensure and practice privilege requirements under the same circumstances.

Working group members noted that this approach would minimize the risk to California consumers and would also address the needs of those consumers who have recently moved to California from another state and would like to continue receiving tax return preparation services from the same public accounting professionals that prepared their tax returns in prior years.

Attached for consideration and action is draft statutory language to implement this approach.

Attachment

Proposed Business and Professions Code Section 5054.

(a) Notwithstanding any other provision of this chapter, an individual or firm holding a valid and current license, certificate, or permit to practice public accountancy from another state may prepare individual tax returns for natural persons who are California residents without obtaining a permit to practice public accountancy issued by the Board under this chapter or a practice privilege pursuant to Article 5.1 of this chapter provided that the individual or firm does not physically enter California to practice public accountancy pursuant to Section 5051, does not solicit California clients, and does not assert or imply that the individual or firm is licensed or registered to practice public accountancy in California.

(b) The Board may, by regulation, limit the number of tax returns that may be prepared pursuant to subdivision (a).

STATEMENT TO BOARD OF ACCOUNTANCY

BRUCE L. BIALOSKY CPA

MAY 19, 2005

Thank you for the opportunity to speak to you this morning regarding the establishment of practice privilege rules for CPAs doing business in California.

First, let me introduce myself. I have been a CPA in the state of California since 1978. I am a presidential appointee to the U.S. Holocaust Memorial Council. I have never previously made a presentation to the Board of Accountancy on any matter, but felt compelled to on this issue.

The matter I am commenting on affects CPAs from other states that do business in California. I am greatly concerned because I have learned first hand the regard in which other states hold California's rules. In 1979, I moved to Reno, Nevada to enter a business with my family. I established a license in Nevada that I maintained for a long period. I found what California did in regard to its rules for CPAs was much a guiding light for Nevada. Thus, I am concerned that what is established in California will resonate throughout the rest of the states and thus create reciprocal requirements on California CPAs.

I would respectfully request that individual tax returns be exempted from the new practice privilege requirements. Let me outline my rationale.

1. Most states have piggyback systems; thus, the level of knowledge necessary to prepare a return is minimal. For those states, like California, that do not have a direct piggyback system, it has been my experience that state returns receive very little focus with the majority of adjustments being provided for through sophisticated software that most CPAs utilize.

2. If there were no exception for individual tax returns then in a case where a client asks you to prepare their child's simple return from a job while working in college would have to be turned down. The CPA would have to apply to the other state and pay a fee that would make it uneconomic to prepare this simple accommodation to a client.

3. If you were a local practitioner and had someone with a multi-state return you would have to apply to each state making it again uneconomic from a cost and time point-of-view. If you represented, for example, an athlete who has income from multiple states (often 10 or more), the CPA would have to apply to each state and then pass on the fees paid to each state

to the taxpayer. Thus, the client would be driven to a large national firm that is already operating in multiple states and would not have to bear the incremental fees for this particular client. Quite often, the national firm charges higher fees than the local practitioner, thus this would be a disservice to the public.

4. If a client relocates to another state, they may wish to maintain their long relationship with the CPA. This would be jeopardized by the cost and time necessary to apply to the new state.

5. Because of the nature of tax practices today, most every CPA does tax returns for multiple states. It is not unusual for a local CPA to prepare tax returns either to accommodate clients or because of relocations in ten states or more. These states may or may not be consistent between tax years. Each year the CPA would have to apply to each state, pay the fees and charge back to their clients the costs.

I understand the desire and encourage the Board's desire to protect the public. The Board will not be protecting the public either by significantly driving up costs that will be passed on to the public or so limiting the universe of qualified practitioners because of external costs that the market itself will drive up the cost to the public.

Thus, I respectfully request that the Board exempt individual tax returns from the requirement to register for practice privileges and thus set an example for the rest of the United States.

Bruce L. Bialosky, CPA
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State of California Department of Consumer Affairs

CALIFORNIA BOARD OF ACCOUNTANCY
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Attachment 8

DEPARTMENT OF CONSUMER AFFAIRS
CALIFORNIA BOARD OF ACCOUNTANCY

FINAL

MINUTES OF THE May 20, 2005 BOARD MEETING

The Westin Horton Plaza
910 Broadway Circle
San Diego, CA 92101
Telephone: (619) 238-2600
Facsimile: (619) 239-0509

I. Call to Order.

President Renata M. Sos called the meeting to order at 8:55 a.m. on Friday, May 20, 2005, at the Westin Horton Plaza in San Diego and ALJ James Ahler and the Board heard Agenda Item XI.A. The Board then convened into closed session at 9:30 a.m. to deliberate and consider Agenda Items XI.B.-F. The Board reconvened into open session at 10:27 a.m. and adjourned at 12:45 p.m.

Board Members	May 20, 2005
Renata M. Sos, President	8:55 a.m. to 12:45 p.m.
Ronald Blanc, Vice President	8:57 a.m. to 12:45 p.m.
Sally Flowers, Secretary-Treasurer	Absent
Richard Charney	8:55 a.m. to 12:45 p.m.
Ruben Davila	Absent
Donald Driftmier	8:55 a.m. to 12:45 p.m.
Charles Drott	Absent
Sara Heintz	Absent
Gail Hillebrand	8:55 a.m. to 12:45 p.m.
Thomas Iino	Absent
Clifton Johnson	8:55 a.m. to 12:45 p.m.
Olga Martinez	8:55 a.m. to 12:45 p.m.
David Swartz	8:55 a.m. to 12:45 p.m.
Stuart Waldman	8:55 a.m. to 12:45 p.m.

Staff and Legal Counsel

Mary Crocker, Assistant Executive Officer
Patti Franz, Licensing Manager
Michael Granen, Deputy Attorney General, Board Liaison
Greg Newington, Chief, Enforcement Program
LaVonne Powell, Legal Counsel
Michele Santaga, Enforcement Analyst
Theresa Siepert, Executive Analyst
Carol Sigmann, Executive Officer
Liza Walker, Regulation Analyst
Jeanne Werner, Deputy Attorney General, Board Liaison
Aronna Wong, Legislation Analyst

Committee Chairs and Members

Nancy Corrigan, Chair, Qualifications Committee
Harish Khanna, Chair, Administrative Committee

Other Participants

Tom Chenowith
Julie D'Angelo Fellmeth, Center for Public Interest Law (CPIL)
Mike Duffey, Ernst & Young LLP
Bill Gage, Chief Consultant, Senate Business, Professions & Economic Development Committee
Kenneth Hansen, KPMG LLP
Richard Robinson, Big 4 Accounting Firms
Hal Schultz, California Society of Certified Public Accountants (CalCPA)
Jeannie Tindel, California Society of Certified Public Accountants (CalCPA)

II. Board Minutes.

A. Draft Board Minutes of the March 18, 2005, Board Meeting.

The draft Board minutes of the March 18, 2005, Board meeting were adopted on the Consent Agenda. (See Agenda Item XII.B.)

III. Report of the President.

A. Update on the Strategic Plan Progress.

Ms. Sos reported that staff are currently working on recommended modifications to the Board's Strategic Plan. She and Mr. Blanc will be attending a workshop at the Board office on July 27, 2005, to review the draft and make final edits. Ms. Sos noted that the revised Strategic Plan

and they will no longer be provided that information unless they know what to ask.

Mr. Newington clarified that the Board currently has two vehicles by which to volunteer information to consumers, License Lookup and the reception phone area. Both locations prominently communicate the disclosure that the information provided is limited to a period of seven years with the exception of the specific items that Mr. Swartz reported on. Mr. Newington noted that the total volume of long-term probationers is approximately six and several have probation extended due to monetary reasons and payment terms, and not necessarily the egregious nature of the discipline.

It was moved by Mr. Swartz, seconded by Mr. Johnson, and carried to adopt staffs' recommendation. Ms. Hillebrand and Mr. Waldman were opposed.

F. Practice Privilege Task Force (PPTF) (Formerly the Uniform Accountancy Act Task Force – UAA TF).

1. Minutes of the March 17, 2005, Practice Privilege Task Force Meeting.

   The minutes of the March 17, 2005, Practice Privilege Task Force meeting were adopted on the Consent Agenda. (See Agenda Item XII.B.)

2. Report on the May 19, 2005, Practice Privilege Task Force Meeting.

   Ms. Hillebrand reported that at the last Board meeting, the Task Force developed a recommendation to ask NASBA to maintain a public list of the various obligations and requirements different states impose for practice privilege. Staff made that request and NASBA has indicated its intent to make that information available to practitioners across the country.

3. Adoption of Appendix 1 to the Practice Privilege Notification Form.

   Ms. Hillebrand reported that the Practice Privilege is available to two categories of licensees of other states. One option is for licensees who are licensed in a state that NASBA has deemed to be substantially equivalent. The current list of 46 states is provided as Appendix 1. **(See Attachment 11.)** Ms. Hillebrand indicated that the Task Force recommended that the Board adopt this list of substantially equivalent states, and to further delegate to the Executive Officer the responsibility to update this list as changes occur.

It was moved by Mr. Driftmier, seconded by Mr. Swartz, and unanimously carried to adopt NASBA's current list of substantially equivalent states and to delegate the responsibility to the Executive Officer to revise the list as necessary.

4. Consideration of an Approach to Address Issuance of Reports Under the Name of Non-Registered Firms.

Ms. Hillebrand reported that at the last Board meeting, an issue surfaced regarding whether an individual holding a practice privilege would be entitled to sign on behalf of their firm. A firm must be registered in California in order to serve California clients on behalf of the firm. Ms. Hillebrand indicated that the Task Force appointed Ms. Sos and herself to work with staff to evaluate whether there was a solution that would not create more problems than it solved.

Ms. Hillebrand noted that there were a number of very serious issues that were considered by the working group. They noted that registered firms have a variety of obligations and it would be inappropriate for these obligations to be waived simply because the individual held the practice privilege.

However, it was recognized that there is a potentially significant problem for out-of-state tax practitioners who are serving clients that need to file a California tax return. She indicated that the working group chose to recommend to the Task Force and the Board a very limited exception to the requirement to hold a license, practice privilege, or firm registration. The exception would apply to tax returns for natural persons and estate tax returns for persons who were clients at the time of the individual's death. Preparation of those types of returns would not require the practitioner to hold a license or a practice privilege and would not require the firm to hold a California registration if:

- The individual or firm does not physically enter California to practice public accountancy pursuant to Section 5051,
- Does not solicit California clients, and
- Does not assert or imply that the individual or firm is licensed or registered to practice public accountancy in California.

Ms. Hillebrand noted that the Task Force recommended the following change to the language in proposed Section 5054:

* On line three, remove the word "individual," and add the following after "California residents:" "or estate tax returns for the estate of natural persons who were clients at the time of death."

Ms. Hillebrand reported that the Task Force unanimously recommended this language to the Board, however, she wanted to disclose that after the Task Force meeting she received a note from Mr. Iino, who could not attend the Board meeting, indicating that upon further reflection, he would favor expanding the exception to make it broader than just for natural persons. Ms. Hillebrand indicated that this would be inconsistent with the action taken by the Task Force and with the idea that any exception should be as narrowly crafted as possible.

Ms. Sos indicated that the reason that this exception is one that the Task Force is comfortable with is because 99 percent of the comments that the Board has received from the profession and the public is related to this issue. There is a need because of a prior relationship between the practitioner and the client. This very narrow exception is in response to real evidence of potentially unintended burdens that would otherwise be created.

Ms. Hillebrand noted that this is being presented to the Board in the form of a recommendation for a statutory change. Staff advised the Task Force that if this exception is approved today, there is a possibility that the change may be in place with the same effective date as the beginning of Practice Privilege.

Ms. Hillebrand reported that there may be a need for an additional Task Force meeting to work on some Q&As in September if the legislation passes. Ms. Hillebrand thanked the former Chair, the Task Force members, other Board members who contributed when permitted under the Open Meeting Act, and all of the members of the public and the profession who were helpful to the work of the Task Force.

Ms. Sigmann indicated that she had spoken with the consultants from the Senate Business and Professions Committee and they had indicated that there could be a means by which to get this language into statute by the time Practice Privilege is implemented.

It was moved by Mr. Driftmier, seconded by Mr. Swartz, and unanimously carried to adopt the Task Force's recommendation with the changes noted above. (See Attachment 12.)

State of California
Department of Consumer Affairs

California Board of Accountancy
2000 Evergreen Street, Suite 250
Sacramento, CA 95815-3832

Memorandum

Practice Privilege TF Agenda Item III
May 19, 2005

Board Agenda Item VIII.F.4
May 20, 2005

Attachment 12

To : Practice Privilege Task Force Members
Board Members

Date : May 4, 2005

Telephone : (916) 561-1788
Facsimile : (916) 263-3674
E-mail : awong@cba.ca.gov

From : Aronna Wong - Aronna
Legislation/Regulations Coordinator

Subject : Consideration of an Approach to Address Issuance of Reports Under the Name of Non-Registered Firms

At the last Practice Privilege Task Force meeting, it was noted that most financial statement reports issued by licensees and most tax returns prepared by licensees are signed with the firm name. It was also noted that while the practice privilege provisions provide for cross-border practice by individuals, there are no comparable provisions for firms. Consequently, under current law, for a firm to practice public accountancy in California which would include performing activities such as reporting on financial statements or preparing tax returns for individual taxpayers or California companies, the firm would need to register with the Board.

This does not pose a problem for larger firms because most larger firms are already registered and have a presence in California. However, it can be challenging for smaller firms since these firm would have to meet all of California's ongoing registration requirements including the requirement that a partner or shareholder hold a California license.

After discussion, the Task Force concluded the issue needed further consideration and a working group consisting of Renata Sos and Gail Hillebrand was appointed to work with staff to develop a proposal for consideration at the May 2005 meetings of the Task Force and the Board.

After evaluating the possibility of a practice privilege for firms and an expedited procedure for qualifying for firm registration, the working group concluded that because of the numerous statutory requirements that tie to registered firms, neither of these two options was practical. During the discussion it was also noted that the greatest concern in this area was expressed by tax practitioners.

After discussion, it was concluded the most workable solution would be to carve out a narrow exception from the firm registration requirement. The working group began crafting its proposal by first identifying areas where no exception was possible. It was determined that any time an individual physically enters California to practice public accountancy as an agent of a firm, that individual must be affiliated with a California-registered firm. It was also determined that any time a firm performs financial statement work, there is sufficient consumer risk so that the firm must be registered with the Board.

After further deliberation, the working group concluded that an exception from the firm registration requirement would be reasonable only in those instances in which the practitioner is preparing individual tax returns, does not physically enter California, does not solicit any California clients, and does not assert or imply that the individual or firm is licensed or registered to practice public accountancy in California. It was further concluded that, for consistency, it would also be appropriate to provide an exception from the individual licensure and practice privilege requirements under the same circumstances.

Working group members noted that this approach would minimize the risk to California consumers and would also address the needs of those consumers who have recently moved to California from another state and would like to continue receiving tax return preparation services from the same public accounting professionals that prepared their tax returns in prior years.

Attached for consideration and action is draft statutory language to implement this approach.

Attachment

Proposed Business and Professions Code Section 5054.

(a) Notwithstanding any other provision of this chapter, an individual or firm holding a valid and current license, certificate, or permit to practice public accountancy from another state may prepare individual tax returns for natural persons who are California residents without obtaining a permit to practice public accountancy issued by the Board under this chapter or a practice privilege pursuant to Article 5.1 of this chapter provided that the individual or firm does not physically enter California to practice public accountancy pursuant to Section 5051, does not solicit California clients, and does not assert or imply that the individual or firm is licensed or registered to practice public accountancy in California.

(b) The Board may, by regulation, limit the number of tax returns that may be prepared pursuant to subdivision (a).

California Society Certified Public Accountants

February 6, 2006

Ronald Blanc, Esq., President
California Board of Accountancy
2000 Evergreen Street, Suite 250
Sacramento, CA 95815

Dear President Blanc and Members:

The rationale provided for development of California's practice privilege statute was to accommodate the need for expedited movement of partners to comply with Sarbanes-Oxley's requirements for audit partner rotation and to respond to a Government Accountability Office study that found the need to comply with different licensing requirements in different states makes it more difficult for smaller firms to compete with the very largest firms. The Board's UAA Task Force and later the Practice Privilege Task Force attempted to "see if an approach to cross-border practice can be developed that is consistent with the Board's consumer protection mission." *Page 2 of the UAA Task Force's December 17, 2003 minutes*. The goals were ease of entry and consumer protection.

CalCPA participated in the deliberations on practice privilege and supported the legislation in the hope that through the regulatory process reasonable accommodations could be made to protect the public interest while facilitating the cross-border accounting practices. However, we now believe that implementation issues, misunderstandings and the impact of unintended consequences require immediate action to rectify what has become an untenable situation for California taxpayers, the entire CPA profession and its foreign counterparts. To this end we ask your support of AB 1868.

It should be remembered that the goals were ease of practice across state lines and increased consumer protection, but California's attempted implementation of practice privilege has in fact made practice across state lines more difficult. If services are provided by the firm (and most engagements are with a firm), the CBA is requiring the firm to register as a firm with the California Board of Accountancy. Firm registration requires that at least one partner be fully licensed in California. Further, if the firm is a corporation or an LLP, the firm must also register with the Secretary of State. The entire process is costly and time consuming.

In the attempt to streamline the process, accommodate ease of entry, and increase consumer protection, we have come full circle. Now in addition to requiring full licensure and registration for the provision of audit services which was the previous Board policy, the CBA is imposing full licensure and registration for all services.

Full disclosure demands that you be aware of the cost that is being imposed on California

taxpayers who choose to use the services of an out-of-state CPA firm practicing as a professional corporation or a limited liability partnership.

Registration with Secretary of State-	$100 minimum 5 days
Registration with the Franchise Tax Board	$800 (minimum) (unknown Processing time)
California Ethics Exam	$125 for instant grading
Filing application for CA CPA license	$395(unknown processing time)
Firm Registration	$350 (unknown processing time)
Practice privilege for any other CPAs in firm Providing service to California clients	$100 each
Minimum total cost	$1,810

Taxpayers using CPA partnerships will experience a minimum increase of $870.00 due to the licensing/registration fees.

Until the entire application process is completed, a firm may not provide any services to a California client. Business tax returns are due March 15. It is unlikely that a firm could comply with the firm registration requirements even if it wanted to, given the time that it takes the California Board of Accountancy to process applications. Registration is required whether or not the CPA actually enters California. This is unacceptable as a matter of public policy especially since there was no evidence that consumer protection was lacking prior to the creation of the practice privilege.

CPAs providing tax services to California taxpayers are already regulated by the Internal Revenue Service, the Franchise Tax Board and the licensing board of accountancy in their home state. Insertion of the California Board of Accountancy in this scheme becomes over regulation. This issue has been raised in the past and the CBA and the California State Legislature chose to exempt out-of- state CPAs providing tax services to individuals, and Business and Professions Section 5040 was enacted. There is little difference between preparing a business tax return and a personal tax return. Allowing the preparation of personal returns without registration while at the same time requiring registration for business tax returns demonstrates a flawed approach.

A September 27, 2004 memo from Aronna Granick *(now Wong)* indicated that there were three circumstances as approved by the Practice Privilege Task Force and the CBA when an out-of-state CPA would need to seek a California license rather than a practice privilege in order to practice in California:

1) The individual wants to establish his or her principal place of business in California [Business and Professions Code Section 5096(a)]
2) The individual wants to provide services from an office in this state and is not an employee of a California registered firm [Business and Professions Code Section 5096(e)(3).]
3) The individual is the subject of a pending investigation in which the outcome is not likely to be known for some time. This reflects the action of the Practice Privilege Task Force at its meeting of September 9, 2004, based on a recommendation of Gregory Newington, Enforcement Division Chief.

Perhaps it is unintentional, but now anytime a CPA from a non-registered firm provides services to anyone even remotely connected to California, full licensure of at least one partner and firm registration is required.

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The complexity, breadth of reach, inadvertent interference in existing long term client relationships, interference with interstate commerce and artificial impediment to foreign investment are not worth whatever incremental improvement, if any, is achieved in consumer protection.

There is also tremendous confusion with the application of the new law. During previous deliberations and discussions a question was asked about the requirement of a practice privilege permit for litigation support services and expert witness testimony. See September 9, 2004 Enforcement Program Oversight Committee minutes on page 148, where it was reported that expert witness testimony was not considered the practice of public accountancy. However, on Thursday, January 12, 2006, we were informed by CBA staff that litigation support services are indeed considered within the definition of the practice of public accountancy and a practice privilege would be required.

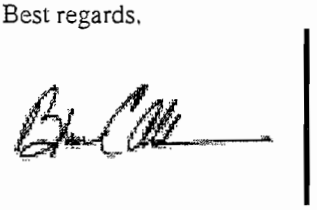
This is an untenable situation for California taxpayers, especially those with multi-state operations. If other states enacted similar provisions, the business owner could be required to retain multiple CPAs to file state tax returns. We agreed that the previous Board policy that required persons and firms providing attest services for California based clients obtain full California licensure needed to be appropriately disclosed and adopted by statute or regulation. We also agreed that a method other than full licensure should be considered for ease of practice. The result even for CPAs providing attest services in California has not eased interstate or international commerce and needs to be immediately corrected.

CPAs across the nation are striving valiantly to comply with the requirements, statutes and interpretations of 54 jurisdictions that do not even agree on what constitutes the practice of public accountancy or what constitutes "Holding Out." We are receiving inquiries from CPAs and organizations throughout the nation raising the issues of constitutionality and impediment to interstate commerce. Additionally, California CPAs are expressing grave concerns as to possible retaliatory action by state boards of accountancy in response to the burdensome California requirements.

California needs to rethink its current approach and act immediately to clean up this confusion. We want to work with the CBA to maintain public protection, but not bar legitimate services being provided to California taxpayers and businesses which operate on an interstate basis and need the professional services of certified public accountants.

It is our hope that the agenda for the February 22nd and 23rd meetings will allow for thorough consideration of all issues related to California's implementation of Section 23. It is our hope that a quick resolution of these issues can be achieved and we can mutually support AB 1868 to provide immediate relief to California taxpayers and the profession.

Best regards,



BRUCE C. ALLEN, Director
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cc: CalCPA Government Relations Committee
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STATE OF CALIFORNIA

Memorandum

TO:	**Carol Sigmann, Executive Officer** **California Board of Accountancy**	Date:	Jan. 9, 2006
		Tel.:	(916) 574 8243
FROM:	**Department of Consumer Affairs** **Legal Office**	Fax:	(916) 574 8623

SUBJ: **Availability of Tax Preparation Exemption for Out-of-State CPAs Employed by Registered Accountancy Firms**

A. ISSUE

In 2005, SB 229 added Business and Professions Code 5054 which creates an exemption from licensure for out-of-state CPAs who prepare tax returns for California citizens. This exemption will apply as long as the individual CPA or the accountancy firm which prepares the tax return is not physically present in this State. A question has arisen as to whether out-of-state CPAs employed by accountancy firms registered in California can qualify for this exemption.

B. CONCLUSION

If the CPA is providing tax returns for clients of an accountancy firm which is registered to do business in California, the exemption found in Section 5054 would not apply.

C. DISCUSSION

B. & P. Code § 5054 (2005 Stats. Ch. 658) provides that:

> *[A]n individual or firm* holding a valid and current license . . . to practice public accountancy from another state may prepare tax returns for natural persons who are California residents . . . without obtaining a permit to practice public accountancy . . . or a practice privilege . . . provided that *the individual or firm* does not physically enter California . . . .

"*The*" individual or firm which cannot enter California is also the same "individual or firm" which is a candidate for an exemption under Section 5054. Thus, the question becomes: Is that same individual or firm physically present in California?[1]

For an individual, the issue of physical presence is a simple one. For firms, it is not. Firms such as corporations or partnerships do not have an individual's "physical presence." So their physical presence must be measured by the level of their business activities. (*International Shoe v. State of Washington*, 326 U.S. 310, 316 (1945); Corp. Code § 15700.) When those activities are "sufficiently substantial and [of a] continuous nature," the corporation or partnership "is treated as if it had a ""physical presence"' in the [state]." (*Serafini v. Superior Ct*, 68 Cal. App. 4th 70, 79 - 80, 80 Cal. Rptr. 2d 159 (1998).)

The standard used to establish physical or economic presence is the same as that for determining whether a firm is subject to the general jurisdiction of the courts of the State. "The standard for establishing general jurisdiction . . . requires that the defendant's contacts be of the sort that approximate physical presence." (*Bancroft & Masters, Inc. v. Augusta National Inc.*, 223 F.3d 1082, 1086 (9th Cir. 2000).) "[E]conomic presence within the state [is] equated with physical presence for jurisdictional purposes." (*Messerschmidt Development Co., Inc. v. Crutcher Resources Corp.*, 84 Cal. App. 3d 819, 824, 149 Cal. Rptr. 35 (1978).) Thus, the standard used by the courts to establish economic or physical presence or general jurisdiction is that the firm's activities are "substantial . . . continuous and systematic." (*Perkins v. Benguet Mining Co.*, 342 U.S. 437, 447 – 448 (1952); *Gates Learjet Corp. v. Jensen*, 743 F.2d 1325, 1331 (9th Cir. 1984).)[2]
Occasional or infrequent business activity will not suffice. For example, in *Cornelison v. Chaney*, 16 Cal. 3d 143, 127 Cal. Rptr. 352 (1976), an out-of-state trucker caused the death of a California citizen, but the accident occurred in Nevada.

---

[1] Nothing in this memorandum should be construed to require the activity of a firm or individual to reach the level of "physical presence" in the State of California before licensure is necessary. B. & P. Code § 5050 prohibits the unlicensed practice of public accountancy. That threshhold is crossed at a much lower level than what is required for physical presence. What that threshhold is need not be analyzed for the purposes of this memorandum.

[2] Physical presence should be contrasted with minimum contacts in a state *related to a cause of action* brought against an out-of-state defendant. This is known as specific as opposed to general jurisdiction. Under that doctrine, the defendant must "purposefully avails itself of the privilege of conducting activities within the forum State, thus invoking the benefits and protections of its laws." *Hanson v. Denckla*, 357 U.S. 235, 253 (1958). Accordingly, a licensed corporation or partnership could be characterized as one that "purposefully avails itself" of "the privilege of conducting [business] within the forum State" and thus subject to specific, but not necessarily general jurisdiction.

His business activity in California consisted of some 20 trips a year into the state over seven prior years. He also had an independent contractor relationship with a local broker and a Public Utilities Commission license. The California Supreme Court rejected plaintiff's attempt to assert general jurisdiction over him. (16 Cal. 3d at 149.) In a footnote, the Court observed that:

> Plaintiff argues that the existence of the Public Utilities Commission license is alone sufficient to justify jurisdiction. However, the fact that defendant had such a license is not determinative but only one factor to consider in evaluating his relationship to this state. (*Id.* at 149, n. 6.)

Applying these principles, it would appear extremely unlikely that a registered firm conducting the practice of accountancy in California could claim that it was not physically present in this State. For example, when a partnership "engage[s] in the practice of accountancy" in California, it must be registered with the Board. (B. & P. Code § 5072(a).) It must also have:

> At least one general partner shall hold a valid permit to practice as a certified public accountant, public accountant, or accountancy corporation, or shall be an applicant for a certificate as a certified public accountant under Sections 5087 and 5088. (B. & P. Code § 5072(b).)

One can thus infer that if a partnership is registered, it is doing business in this State on a continuous basis and acting through at least one general partner who is a California licensed CPA.

Likewise, an accountancy corporation registered with the Board must do so pursuant to the Moscone-Knox Professional Corporation Act . . . . (B. & P. Code § 5150.) Under that Act:

> A professional accountancy corporation is one "that is engaged in rendering professional services." (See Corp. Code § 13401(b).)

For a limited liability partnership:

> [A] partnership . . . . shall file with the Secretary of State a registration . . . stating the following: (1) The name of the partnership. (2) The address of its principal office. (3) The name and address of the agent for service of process on the limited liability partnership in California. (4) A brief statement of the business in which the partnership engages . . . . (Corp. Code § 16953.)

Thus, any accountancy firm which is registered with the Board is probably doing business in California on a "substantial . . . continuous and systematic" basis. If that is the case, it would then be physically present in this State.

Accordingly, a CPA licensed in another state and employed by a firm registered in California would not be able to qualify for an exemption under Section 5054 if he or she prepared a tax return for one of his or her firm's California clients. The reason is that the CPA is not acting in his or her individual capacity, but as an agent of the firm. Even though he or she might be absent from California, his or her registered firm is not. Because the firm, not the individual, is the entity legally recognized as doing the tax preparation work, the requirements of 5054 would not be met.

There are obvious exceptions. For example, if the CPA were "moonlighting" and prepared a tax return for a California resident who is not a client of the firm, then the presence of the firm is immaterial. The CPA is now acting in his or her individual capacity rather than as the agent of the firm. As long as the CPA does not physically enter the State, he or she should be able to qualify for the exemption under Section 5054.

DOREATHEA JOHNSON
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Attachment 11

February 2, 2006

Ronald Blanc, Esq.
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Gail K. Hillebrand, Esq.
Chair, Committee on Professional Conduct
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Dear Mr. Blanc and Ms. Hillebrand:

At the request of the executive officer, Ms. Sigmann, I write to elaborate on several issues, relating to the new practice-privilege regime, that were raised at the January meetings of the Board and its Committee on Professional Conduct.

As you know, new California legislation and regulations, effective January 1, 2006, have created a practice privilege, pursuant to which qualified accountants licensed in other U.S. States may practice temporarily in California with notice to the Board of Accountancy. The Board staff has developed and posted on the Board's Internet site a "Practice Privilege Handbook" designed to guide out-of-state accountants through the process of determining their eligibility for the practice privilege and submitting their applications.

The initial implementation of the practice privilege has raised some significant issues. I appreciate this opportunity to offer some comments and concerns, on an expedited basis. I look forward to working with the Board to address these issues and improve the administration of the practice-privilege regime going forward.

I. Temporary Practice by Foreign Accountants

One of the most important temporary-practice issues left outstanding is the need to allow licensed foreign accountants to work in California on matters relating to their regular overseas practice for brief periods of time. The practice-privilege system is not open to accountants licensed in other countries, who historically have been covered by a statutory exemption for temporary, incidental practice. That statutory provision was inadvertently repealed. I strongly support the Board's unanimous decision, at its January meeting, to seek legislation to make clear that licensed foreign accountants still are permitted to engage in this limited form of practice.

II. Nonresident Tax Preparer Exemption

The Legislature has created a special rule for accountants who prepare tax returns for individual clients. Pursuant to Section 5054(a), an accountant who does not work in California or solicit clients in California may prepare tax returns for individual California clients without obtaining either a California license or a practice privilege. This exemption is a sensible one: it effectively preserves existing relationships between individual clients and properly licensed accountants, while ensuring that the practice privilege remains the primary method for out-of-state accountants to engage in limited practice in California.

I am concerned by the Board staff's initial interpretation of Section 5054(a), which appeared to limit the exemption for individual tax preparation in ways that the Legislature did not intend. The Board itself has not promulgated any regulations construing Section 5054(a). The Practice Privilege Handbook, however, seemed to take the position that an out-of-state accountant may not claim the benefit of this exception if he is employed by a *firm* that is registered in California, even if he does not work in California or solicit California clients.

An early version of the Practice Privilege Handbook read as follows:

> Q: I am an out-of-state CPA employed by a California licensed firm. Under the tax exception referenced in Section 5054 of the California Accountancy Act, can I sign individual (natural person) tax returns without a California Practice Privilege or California CPA license?
>
> A: *No, the firm has a physical presence in California by virtue of being registered in California. Since the firm is the entity legally recognized as doing the tax return, the exception of Section 5054 would not apply.* As a signer, you would be required to obtain a California Practice Privilege or a California CPA license.
>
> Q: I am employed by of an out-of-state CPA firm. The firm is divided into 2 divisions. One division is responsible for providing attest services in California and the other division is responsible for tax returns. The employees in the tax division have California clients who are individuals (natural persons) and the employees of this division do not physically enter California. What do the out-of-state CPAs in the tax division need under California requirements?
>
> A: California law treats a firm as a single entity regardless of how the firm is structured. The firm, through its attest services, is now physically entering California and is required to register with the California Board of Accountancy. *The out-of-state CPAs signing the individual (natural person) tax returns on behalf of the firm would now be required to obtain a California Practice Privilege or a California CPA license since the firm has a physical presence in California.*

Former Practice Privilege Handbook at 19-20 (emphases added).

I am pleased to see that these examples have been removed from the Practice Privilege Handbook as of January 26, 2006. The Handbook now merely restates the statutory text. *See* Practice Privilege Handbook at 19, 20.

As set forth below, it appears that an interpretation of Section 5054 that would preclude accountants in registered firms from using that provision would not be the best reading of the statutory text, would not effectuate the Legislature's intent, and would not serve the public policy goals of the Board or the Legislature. An individual accountant who complies with the provisions of Section 5054—provisions that encompass only a relatively small number of accountants—should not be subject to the additional requirement of filing for a California practice privilege or license.

A. Statutory Text

The text of Section 5054 permits "an individual or firm" to engage in this limited form of tax practice, provided that "the individual or firm" meets certain conditions. The structure of the section makes clear that an individual can invoke this provision even if affiliated with a firm. Thus, "an individual" who is licensed and in good standing in another State may prepare tax returns for an individual Californian if "the individual" meets the three conditions, *i.e.*, if he "does not physically enter California," "does not solicit California clients," and "does not assert that the individual . . . is licensed . . . to practice public accountancy in California."

Although the individual accountant in the Practice Privilege Handbook's now-removed examples had met each of these three conditions, the Handbook maintained that "the firm is the entity legally recognized as doing the tax return," Former Practice Privilege Handbook at 19, and that the *accountant* therefore must obtain a practice privilege. The Handbook did not cite any California law establishing this proposition, and even if it is accurate as a general matter, Section 5054 affirmatively provides that an individual accountant "may prepare" tax returns for individuals "[n]otwithstanding any other provision of" the accountancy statutes.

Especially if the return is issued under the individual accountant's name, there should be no doubt that the accountant is entitled to use the limited exception set out in Section 5054. Even if the tax return is issued in the name of the firm, that does not trigger an obligation for the individual CPA to seek a practice privilege. The individual CPA has still complied with all of the conditions of Section 5054, and therefore remains exempt from the requirement to obtain a license or a practice privilege. As for the firm, in the examples it has already registered with the Board, so it has satisfied its own obligations.

The deleted answers in the Practice Privilege Handbook apparently were based on two assumptions: that if the accountant's firm is registered in California, the firm has "physically enter[ed] California to practice public accountancy," and that if the firm has physically entered California, then the individual accountant is also deemed to have entered California. I disagree with these assumptions. First, although a firm that applies for registration certainly submits to the regulatory jurisdiction of the Board, the statute uses the specific term "physically enter California," which appears to require more than just filing for registration. Second, even if the firm has "physically enter[ed]" the State, it does not follow that the individual accountant is also deemed to have entered—and disqualified himself from invoking Section 5054.

As discussed above, the conditions in Section 5054 can apply to "the individual" on his own, without regard to "the firm," thus permitting "the individual" to invoke the section's exception for tax practice.[1]

B. Legislative Intent

What little legislative history is available strongly suggests that the Legislature intended to allow qualifying accountants to engage in limited tax practice pursuant to Section 5054, whether or not they are associated with a registered firm. The floor analyses prepared for both the Senate and the Assembly stated that the new section would allow an accountant to provide tax services to individuals "without a California license, a practice privilege, or a public accounting firm employer registered in California." Senate Floor Analysis at 5; Assembly Floor Analysis at 2. Plainly, therefore, the Legislature intended that an accountant could practice pursuant to Section 5054 without applying for licensure; securing a practice privilege; or establishing a relationship with a registered firm, presumably to fit within the supervised-practice exception of Section 5053.

C. Public Policy

Reading Section 5054 to treat an accountant's association with a registered firm as disqualifying would be not only inconsistent with the Legislature's intent, but also contrary to sound public policy. That approach would treat an out-of-state accountant much less favorably if he works for a registered firm. An out-of-state accountant who does not work for a registered firm can engage in limited tax practice under Section 5054, provided that he meets the three conditions. If he works for an unregistered firm, that status is no obstacle; indeed, the Board does not require that an accountant work for a firm that is registered or licensed *anywhere* in order to invoke Section 5054.

This disparate treatment would be inappropriate. Accountants who work for registered firms belong to institutions that have submitted to the California Board's jurisdiction, satisfied the requirements for registration, and remained in good standing. California-registered firms are also subject to various reporting requirements, pursuant to which they disclose professional discipline, civil judgments related to professional conduct, and government investigations involving their accountants. *See* CAL. BUS. & PROF. CODE § 5063.

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[1] Indeed, the structure of the statute demonstrates that Section 5054 cannot be read to bar "an individual" from engaging in limited tax practice if "the firm" has entered California. If each of the references to "the individual or firm" in Section 5054 were read consistently with that interpretation, the statute would bar "an individual" associated with a registered firm from telling his clients "that the . . . firm is licensed or registered to practice public accountancy in California," even though that information would be both true and valuable. That individuals associated with registered firms cannot logically be barred from invoking Section 5054 without also yielding this absurd result, provides an additional reason not to adopt this strained interpretation of the text.

Section 5054 was designed to *allow* this type of accountant to continue to service clients in California. These accountants should not receive less favorable treatment than accountants who work for unregistered firms. Such an exclusion would cause an unnecessary disruption of the client relationship without improving client service.

D. Recommendation

Accordingly, the Board should make clear that any individual accountant who meets Section 5054's three conditions may engage in the form of limited tax practice described in that statute. If the accountant does not physically enter California, does not solicit California clients, and does not hold himself out as a California licensee, Section 5054 permits him to prepare tax returns for individual Californians, irrespective of whether he is employed by a registered California firm.

III. Application of Practice-Privilege Requirement to Out-of-State Work

I am also concerned by the Practice Privilege Handbook's treatment of other accounting work, such as audits, that occurs entirely outside California. Several of the Q&A illustrations in the Practice Privilege Handbook assert that an accountant must obtain a California practice privilege to service "clients who reside in California," even if no work is actually performed in California. Previously, the Practice Privilege Handbook had used the much more vague formulation "a California client" instead of "clients who reside in California." I strongly support the deletion of the concept of "a California client": that term does not appear in the governing statute or regulations; the Handbook did not define it; and, in fact, the Handbook contained conflicting suggestions as to what might constitute "a California client."

While I applaud the removal of this vague concept and believe that the new formulation of "clients who reside in California" is a step in the right direction, I still have some concerns about the specificity of the new language as well as its basis. I discuss these concerns below.

As revised, the Practice Privilege Handbook states:

> Q: I'm a CPA in another state and do not plan to be in California. I do only one tax return for a California client. Do I need a California practice privilege?
>
> A: Yes, in order to provide public accounting services to *clients who reside in California* you will be required to obtain a California practice privilege or obtain a California CPA license. Preparing tax returns as a CPA is a service that falls within the definition of the practice of public accountancy contained in Section 5051 of the California Accountancy Act.
>
> * * * *

> Q: I'm a CPA in another state. One of my clients retired and moved to California. Do I need a practice privilege to continue to prepare that client's tax return?
>
> A: Yes, in order to provide public accounting services to *clients who reside in California* you will be required to obtain a California practice privilege or obtain a California CPA license. Preparing tax returns as a CPA is a service that falls within the definition of the practice of public accountancy contained in Section 5051 of the California Accountancy Act.
>
> * * * *
>
> Q: I am a Utah CPA who prepares state tax returns filed with the California Franchise Tax Board for my Utah resident clients. Do I need a practice privilege after December 31, 2005?
>
> A: No. However, you would need to obtain a California practice privilege or obtain a California CPA license to practice public accountancy as defined in Section 5051 of the California Accountancy Act if you intend to service *clients who reside in California.*
>
> * * * *

Practice Privilege Handbook at 19-20 (emphases added).

As discussed below, the term "clients who reside in California" is not drawn from the governing statute and is not defined in regulations or other Board guidance. I am concerned that using this vague concept to determine when an out-of-state accountant must file for a practice privilege will cause uncertainty, both about the accountant's duty to seek a privilege and about the Board's statutory and constitutional authority to adopt such a potentially far-reaching rule.

A. Undefined Standard

The Practice Privilege Handbook does not define what determines whether a business "resides in California." Nor do the California accountancy statutes or regulations, which do not use the concept to refer to businesses. (Section 5054 uses the concept to apply only to natural persons.)

Indeed, the Practice Privilege Handbook offers somewhat conflicting indications as to what may constitute a business client that resides in California. In one example, the Handbook suggests that if a client's "primary business operation" is in California but its "administrative office" is not, the accountant need not obtain a California practice privilege unless he "physically enters California to practice public accountancy." Practice Privilege Handbook at 21. It is unclear, however, whether the Practice Privilege Handbook means to establish definitively that a business "resides" only in the State where its "administrative office" is located.

B. Statutory and Constitutional Concerns

The basis for the requirement that an accountant seek licensure or a practice privilege is Section 5050. That section requires an accountant to obtain a practice privilege or a California CPA license only if he seeks to "engage in the practice of public accountancy *in this state*" (emphasis added). Although the statute defines "practice of public accountancy," it does not define "in this state," and thus gives that term its ordinary meaning.

Merely servicing "clients who reside in California" does not in all cases constitute practicing public accountancy "in this state," as that term is ordinarily read or understood. The statute evidently makes the location of the services the critical factor, not the location of the client. The definition of public accountancy includes, for example, "perform[ing]" or "render[ing] professional services to clients for compensation." CAL. BUS. & PROF. CODE § 5051(c), (e). If no service is "perform[ed]" or "render[ed]" in California, then it would appear that the accountant is not practicing public accountancy in California ("in this state") and should not need to obtain a practice privilege or a license.

Were the Board to enforce the practice-privilege requirement as the Practice Privilege Handbook suggests, it would be regulating the conduct of accountants who have no contact with California. Indeed, it would absolutely forbid these accountants from accepting specified engagements under certain circumstances, potentially even if the client's entire business operation were located in another State and the work were performed entirely in that other State. The Federal Constitution limits a State's power to regulate beyond its borders in this fashion. The U.S. Supreme Court has struck down state regulations that seek to "project" the State's own regulatory regime onto businesses in other States. The interpretations suggested in the Handbook implicate and may exceed these constitutional limits. In the face of such serious constitutional questions, the Board should avoid such a broad interpretation, especially as the statutory text supports a far narrower view.

C. Conflict with Other States' Regulation of Accountancy

Requiring a California practice privilege is not necessary to ensure that services provided to California licensees will be regulated. Any accountant who provides services outside California will be regulated by the State of licensure. For the Board to insist that accountants who never enter the State also obtain a practice privilege in California, merely because the client has operations there, would only further complicate the regulatory framework with which accountants must comply.

The National Association of State Boards of Accountancy (NASBA) is in the process of addressing the complexities of multistate regulation, including issues like this one. NASBA and the AICPA have recently promulgated a new version of the Uniform Accountancy Act, Section 23 of which includes a substantial-equivalency provision similar to the practice-privilege legislation that California adopted. The UAA requires the State of licensure to receive and address disciplinary concerns raised by other jurisdictions. *See* UNIF. ACCOUNTANCY ACT § 23(b).

The NASBA committee that drafted the UAA will be meeting over the coming year to draft implementing regulations, which will likely address any potential regulatory conflicts and clarify which State should be primarily responsible for regulating an audit engagement that occurs in multiple places. While this process is ongoing, the Board should not take any steps that disrupt the current system of regulation by the State of licensure and the State where services are rendered. It would be appropriate for the Board to revisit the issue next year, once the new UAA rules have been promulgated and the Board has had a chance to determine whether they adequately address the issue of regulating multistate practice. The next year will also give the Board experience with the operation of the practice privilege in California and allow it to assess how frequently this issue arises.

D. Recommendation

At least for the first year that the new practice privilege is in effect, the Board should enforce the statutory requirement, which requires an accountant to obtain a practice privilege only when the accountant physically enters California to practice public accountancy. The Committee and the Board should not ratify the Handbook's vague concept of a "client who resides in California," which suffers from a lack of clarity and from the potential defects of statutory and constitutional authority identified above. The Board will be able to revisit the issue next year with more information at its disposal, once regulations to implement Section 23 of the revised UAA have been developed.

IV. Applicants from Non-Substantially Equivalent States

Applicants for a practice privilege must demonstrate in one of three ways that they possess credentials that are "substantially equivalent" to a California licensee's: they may show that they were licensed by a state recognized as substantially equivalent; that they have "continually practiced public accountancy . . . for at least four of the last ten years"; or that their individual qualifications are substantially equivalent to California's standards. CAL. BUS. & PROF. CODE § 5096(a). The statute allows the Board to determine how an applicant may demonstrate sufficient individual qualifications. *See id.* § 5096(a)(3), (b). By regulation, the Board has provided that an accountant may have his credentials verified by CredentialNet, which is operated by NASBA. CAL. CODE REGS. tit. 16, § 27(b).

I agree with the Board that approval by CredentialNet should be sufficient to demonstrate the qualifications for a practice privilege. I am concerned, however, about the potential delay in the process caused by CredentialNet. Under the regulations, an accountant must actually "obtain the required substantial equivalency determination" from CredentialNet "[p]rior to seeking a practice privilege." *Id.* One great benefit of the practice-privilege system is the flexibility it allows out-of-state accountants to travel to California on short notice, to notify the Board on a relatively simple and straightforward form that can be submitted electronically, to pay the applicable fee at any time within 30 days, and to begin practicing no later than the time of submission (and up to five days earlier, pursuant to the safe-harbor provision that is in effect for 2006 and 2007, *id.* § 30). The regulations, however, deny this flexibility to an accountant who is licensed by a State that is not recognized as "substantially equivalent" and who does not meet the four-years-in-ten qualification, even if his individual credentials are unquestionably within

California's standards. He may not seek the practice privilege until NASBA has completed his paperwork. If he may not obtain the practice privilege, he may not practice public accountancy in California.

The statute and regulation allow the Board to determine what individual qualifications meet the standard of substantial equivalency; neither the Legislature nor the Board has suggested that the CredentialNet evaluation should be the exclusive means of demonstrating appropriate qualifications. *See* CAL. BUS. & PROF. CODE § 5096(a)(3); CAL. CODE REGS. tit. 16, § 27(b). I note that Section 23(a)(2) of the Uniform Accountancy Act contains a "grandfather clause" allowing the Uniform CPA Examination to substitute for other credentials until the year 2012, by which time those States that are not yet substantially equivalent are expected to have upgraded their requirements to meet that standard.

It would be appropriate for the Board to add the Uniform CPA Examination to § 27 as an alternative measure of qualifications. Indeed, a candidate who has already passed the Uniform CPA Examination has already met the primary qualification for licensure. *See* CAL. BUS. & PROF. CODE §§ 5092(c), 5093(c); CAL. CODE REGS. tit. 16, § 6. NASBA's Uniform Accountancy Act recognizes that a satisfactory test score justifies excusing an applicant from the requirement that he have completed a set number of hours of education, *see* UNIF. ACCOUNTANCY ACT § 23(a)(2). For the same reason, a satisfactory test score justifies excusing an applicant for a practice privilege from rote compliance with the four-years-in-ten requirement.

V. Notification of Routine Renewals

The Board's approved notification form includes a space for the out-of-state accountant to fill in the expiration date of his current accountancy license. This information is not part of the public record, however. *See* Practice Privilege Handbook at 10. Rather, only the State of licensure is made public, *see id.*, so a member of the public seeking to verify that a holder of a California practice privilege is still in good standing in the State of licensure would have to check with that State. Holders of a practice privilege agree to keep the Board informed of any change to the information reported on the notification form within 30 days. CAL. CODE REGS. tit. 16, § 33.

The Practice Privilege Handbook provides:

> If the CPA license identified in the Notification Form used as the basis for qualifying for a California Practice Privilege is renewed during the term of an individual's California Practice Privilege, it must be reported to the Board through your online client account or in writing within 30 days of the renewal date. An individual may be subject to a fine of $250 to $5,000 for failure to comply with this requirement.

Practice Privilege Handbook at 11. Thus, even if the accountant remains in good standing, and the State of licensure and the license number remains unchanged, the Practice Privilege Handbook requires notification even of a routine renewal.

This requirement creates an unnecessary burden on holders of the practice privilege. For an accountant in good standing, renewals are routine events, and in some cases may even be handled primarily by administrative or compliance personnel. The Board would be able at all times to verify the status of any accountant who holds a practice privilege: applicants agree "[t]o respond fully and completely to all inquiries" by the Board and to allow the Board to contact any other state agencies concerning their credentials. And the holder of a privilege, like a licensee, would still be obliged to report to the Board any "refusal to renew a certificate" or other termination of the right to practice by the State of licensure. CAL. BUS. & PROF. CODE §§ 5063(a)(2), 5096.7(a). Finally, as noted above, requiring the licensee to submit regular reports would not benefit California consumers, because the expiration date would not be public information in any event.

Therefore, the Board should refrain from requiring holders of a practice privilege to submit additional notifications each time they renew their licenses in their home States. Rather, licensees should be obliged to notify the Board only if their status as a licensee in good standing changes.

VI. Disqualifying Conditions

The Board has appropriately exercised its authority to clarify the statutory list of disqualifying conditions and to make appropriate *de minimus* exceptions. As the Board has recognized, it is important to make the list of disqualifying conditions as straightforward and easy to comprehend as possible, so that no accountant mistakenly thinks that he is not subject to a disqualifying condition and accordingly attempts to practice pursuant to the privilege without Board approval.

In that spirit, I offer a few additional areas in which further clarification is warranted.

A. Investigations

I recommend clarifying the disqualifying condition relating to pending investigations. In particular, I note that the SEC and PCAOB make a practice of notifying accountants or firms that they are implicated in formal investigations. *See, e.g.*, PCAOB Rule 5101. These agencies sometimes receive complaints against accountants, which are quickly dismissed after preliminary inquiry and without the need for a formal order of investigation. Indeed, in some such instances the subject of the complaint is not formally notified of the inquiry.

The Board should take the position that a pending investigation by the SEC, PCAOB, or other agency that uses the same procedure is a disqualifying condition only if the SEC, PCAOB, or other agency has issued a formal order of investigation that names the accountant seeking or holding the practice privilege. Such a position would be entirely consistent with legislative intent; when the Legislature wants to include preliminary stages of inquiry that occur before a formal investigation, it knows how to do so. *See, e.g.*, CAL. BUS. & PROF. CODE § 5063(b)(3)-(4) (requiring licensees to notify the Board of any formal order of investigation by the SEC *or* of any invitation to make a Wells submission, which occurs before the SEC issues a formal order). No such language appears in Section 5096(g)(2), which sets out the list of disqualifying conditions.

The Board should also amend Section 32(c)(3) of the regulations to clarify that the pendency of an informal inquiry by the PCAOB staff, pursuant to PCAOB Rule 5100, is not a disqualifying condition.

B. Duration of Privilege Following Resolution of Disqualifying Conditions

A practice privilege lasts for one year from its effective date, unless the holder of the privilege files a new notification form or receives a California license. CAL. CODE REGS. tit. 16, § 29(b)-(c). In general, as the Board's regulations recognize, the year should run from the date the notification form is filed, because that is the date that the practice privilege becomes effective.

The Practice Privilege Handbook takes the position that when approval of the practice privilege is delayed because the Board must consider a disqualifying condition, the delay counts against the privilege holder's one year. *See* Practice Privilege Handbook at 17 ("Your California Practice Privilege term still expires one year from the date of submission of the Notification Form and is not extended by a delay in your receiving practice rights.") The Board should clarify Section 29 of the regulations to make plain that the one year runs from the effective date of the privilege even if the privilege is not effective upon the filing of the notification. For example, if an accountant has one of the specified disqualifying conditions and must seek the Board's approval to obtain a practice privilege, the Board may take some time to consider and process his request. During that time, the accountant cannot practice in California. The one-year practice privilege therefore should begin when the accountant receives permission to practice.

Clarifying the regulation and specifying that, when Board approval is required, the one year begins when the Board approves the application, would benefit both accountants and the Board by reducing the need to submit and process duplicative filings. There is no need to impose a shortened renewal deadline on accountants once Board approval is granted; holders of a practice privilege, of course, remain obliged to notify the Board if any new disqualifying condition arises or if any of the information in their applications change. *Id.* §§ 32(b), 33.

C. Renewal of Privilege Following Resolution of Disqualifying Conditions

A practice privilege expires after one year but may be renewed upon submission of a new notification form. There is an ambiguity in the regulations concerning renewals of practice privilege by applicants who previously were the subject of a disqualifying condition, but who were granted a practice privilege by the Board.

For example, suppose that the Board grants a practice privilege to an accountant who was convicted of a petty offense while in college, and who properly disclosed that conviction on his notification form pursuant to Section 32(c)(1) of the regulations. When that accountant applies for a new practice privilege, may he commence practice immediately upon notification, or must he again await Board approval because of his past disqualifying condition?

An appropriate answer can be found in line F of the "Disqualifying Conditions" section of the notification form. That line asks the applicant whether he has previously been notified by the Board "that prior Board approval is required before practice under a new practice privilege may commence."

The Board should adopt a practice, whenever it approves an application for practice privilege by an accountant with a disqualifying condition, of notifying the applicant whether he must seek Board approval before applying again for a practice privilege. In the above example of the past conviction for a petty offense, for instance, it would be appropriate to inform the applicant that he may apply in the future for a practice privilege without Board approval—unless, of course, a new disqualifying condition arises before that time.

This letter is not intended to be an all inclusive list of issues raised by the handbook, the FAQs contained therein or the regulations as interpreted by the forgoing documents.

As I stated at the last board meeting, I appreciate the efforts of the board and its staff to address these very serious issues. I look forward to continuing our discussions at the next board meeting. In the meantime, if I can answer any questions please do not hesitate to contact me.

Sincerely,

Richard Robinson

cc: Carol Sigmann

BUSINESS AND PROFESSIONS CODE SECTIONS 5035.2, 5050-5051

5035.2. "Client", as used in any context in this chapter, means any person for whom public accountancy services are performed or to whom financial products, financial services, or securities are sold or provided at the licensee's public accountancy practice or through referral to any other location or business in which the certified public accountant has a material interest.

5050. (a) No person shall engage in the practice of public accountancy in this state unless the person is the holder of a valid permit to practice public accountancy issued by the board or a holder of a practice privilege pursuant to Article 5.1 (commencing with Section 5096).

(b) This section shall become operative on January 1, 2006.

5051. Except as provided in Sections 5052 and 5053, a person shall be deemed to be engaged in the practice of public accountancy within the meaning and intent of this chapter if he or she does any of the following:

(a) Holds himself or herself out to the public in any manner as one skilled in the knowledge, science, and practice of accounting, and as qualified and ready to render professional service therein as a public accountant for compensation.

(b) Maintains an office for the transaction of business as a public accountant.

(c) Offers to prospective clients to perform for compensation, or who does perform on behalf of clients for compensation, professional services that involve or require an audit, examination, verification, investigation, certification, presentation, or review of financial transactions and accounting records.

(d) Prepares or certifies for clients reports on audits or examinations of books or records of account, balance sheets, and other financial, accounting and related schedules, exhibits,

statements, or reports that are to be used for publication, for the purpose of obtaining credit, for filing with a court of law or with any governmental agency, or for any other purpose.

(e) In general or as an incident to that work, renders professional services to clients for compensation in any or all matters relating to accounting procedure and to the recording, presentation, or certification of financial information or data.

(f) Keeps books, makes trial balances, or prepares statements, makes audits, or prepares reports, all as a part of bookkeeping operations for clients.

(g) Prepares or signs, as the tax preparer, tax returns for clients.

(h) Prepares personal financial or investment plans or provides to clients products or services of others in implementation of personal financial or investment plans.

(i) Provides management consulting services to clients.

The activities set forth in subdivisions (f) to (i), inclusive, are "public accountancy" only when performed by a certified public accountant or public accountant, as defined in this chapter.

A person is not engaged in the practice of public accountancy if the only services he or she engages in are those defined by subdivisions (f) to (i), inclusive, and he or she does not hold himself or herself out, solicit, or advertise for clients using the certified public accountant or public accountant designation. A person is not holding himself or herself out, soliciting, or advertising for clients within the meaning of this section solely by reason of displaying a CPA or PA certificate in his or her office or identifying himself or herself as a CPA or PA on other than signs, advertisements, letterhead, business cards, publications directed to clients or potential clients, or financial or tax documents of a client.

Section 5050

(a) No person shall engage in the practice of public accountancy in this state unless the person is the holder of a valid permit to practice public accountancy issued by the board or a holder of a practice privilege pursuant to Article 5.1 (commencing with Section 5096).

~~(b) This section shall become operative on January 1, 2006.~~

(b) Nothing contained in this chapter shall prohibit a person who holds an authorization to practice public accountancy from a foreign country, lawfully practicing therein, from temporarily practicing in this State incident to an engagement in that country provided that:

(1) The practice is primarily regulated by the accountant's country of licensure and is performed under accounting or auditing standards of that country; and

(2) The accountant does not hold himself or herself out as being licensed as a Certified Public Accountant or Public Accountant by the State of California.

Section 5088. Interim Practice Rights: Out-of-State Certified Public Accountant – REPEALED

(a) Any person who is the holder of a valid and unrevoked license as a certified public accountant issued under the laws of any state and who applies to the board for a license as a certified public accountant under the provisions of Section 5087 may, after application for licensure and after providing evidence of qualifying continuing education, perform the same public accounting services in this state as a certified public accountant licensed under Section 5092 or 5093 until the time his or her application for a license is granted or rejected.

(b) An applicant meeting the requirements of subdivision (a) who certifies that he or she has met the requirements of Section 5095 may perform attest services in this state until the time his or her application for a license is granted or rejected.

(c) This section shall remain operative until January 1, 2006, and as of that date is repealed.

State of California
Department of Consumer Affairs

California Board of Accountancy
2000 Evergreen Street, Suite 250
Sacramento, CA 95815-3832

Memorandum

CPC Agenda Item III.A.B.C.
February, 22 2006

To : CPC Members

Date: February 15, 2006
Telephone : (916) 561-1788
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E-mail: awong@cba.ca.gov

From : Aronna Wong
Legislation/Regulations Coordinator

Subject : Significant Issues Related to Temporary Practice and/or the Implementation of Practice Privilege

Attached for your consideration are a letter from Richard Robinson to Ronald Blanc, Esq. and Gail K. Hillebrand, Esq. dated February 2, 2006, and a memorandum dated February 9, 2006, containing a legal analysis prepared by Department of Consumer Affairs Staff Counsel, George P. Ritter.

Mr. Robinson's letter raised legal issues related to the Nonresident Tax Preparer Exemption – Business and Professions Code Section 5054 and the Application of Practice-Privilege to Out-of-State Work – Jurisdictional Issues. Mr. Ritter's memorandum speaks to these issues. Mr. Robinson's letter also identified concerns related to applicants from non-substantially equivalent states and notification of routine renewals. These concerns relate more to policy than to legal issues and can be addressed as part of a more detailed policy discussion.

Attachments

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February 2, 2006

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Gail K. Hillebrand, Esq.
Chair, Committee on Professional Conduct
California Board of Accountancy
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Dear Mr. Blanc and Ms. Hillebrand:

At the request of the executive officer, Ms. Sigmann, I write to elaborate on several issues, relating to the new practice-privilege regime, that were raised at the January meetings of the Board and its Committee on Professional Conduct.

As you know, new California legislation and regulations, effective January 1, 2006, have created a practice privilege, pursuant to which qualified accountants licensed in other U.S. States may practice temporarily in California with notice to the Board of Accountancy. The Board staff has developed and posted on the Board's Internet site a "Practice Privilege Handbook" designed to guide out-of-state accountants through the process of determining their eligibility for the practice privilege and submitting their applications.

The initial implementation of the practice privilege has raised some significant issues. I appreciate this opportunity to offer some comments and concerns, on an expedited basis. I look forward to working with the Board to address these issues and improve the administration of the practice-privilege regime going forward.

I. Temporary Practice by Foreign Accountants

One of the most important temporary-practice issues left outstanding is the need to allow licensed foreign accountants to work in California on matters relating to their regular overseas practice for brief periods of time. The practice-privilege system is not open to accountants licensed in other countries, who historically have been covered by a statutory exemption for temporary, incidental practice. That statutory provision was inadvertently repealed. I strongly support the Board's unanimous decision, at its January meeting, to seek legislation to make clear that licensed foreign accountants still are permitted to engage in this limited form of practice.

II. Nonresident Tax Preparer Exemption

The Legislature has created a special rule for accountants who prepare tax returns for individual clients. Pursuant to Section 5054(a), an accountant who does not work in California or solicit clients in California may prepare tax returns for individual California clients without obtaining either a California license or a practice privilege. This exemption is a sensible one: it effectively preserves existing relationships between individual clients and properly licensed accountants, while ensuring that the practice privilege remains the primary method for out-of-state accountants to engage in limited practice in California.

I am concerned by the Board staff's initial interpretation of Section 5054(a), which appeared to limit the exemption for individual tax preparation in ways that the Legislature did not intend. The Board itself has not promulgated any regulations construing Section 5054(a). The Practice Privilege Handbook, however, seemed to take the position that an out-of-state accountant may not claim the benefit of this exception if he is employed by a *firm* that is registered in California, even if he does not work in California or solicit California clients.

An early version of the Practice Privilege Handbook read as follows:

> Q: I am an out-of-state CPA employed by a California licensed firm. Under the tax exception referenced in Section 5054 of the California Accountancy Act, can I sign individual (natural person) tax returns without a California Practice Privilege or California CPA license?
>
> A: *No, the firm has a physical presence in California by virtue of being registered in California. Since the firm is the entity legally recognized as doing the tax return, the exception of Section 5054 would not apply.* As a signer, you would be required to obtain a California Practice Privilege or a California CPA license.
>
> Q: I am employed by of an out-of-state CPA firm. The firm is divided into 2 divisions. One division is responsible for providing attest services in California and the other division is responsible for tax returns. The employees in the tax division have California clients who are individuals (natural persons) and the employees of this division do not physically enter California. What do the out-of-state CPAs in the tax division need under California requirements?
>
> A: California law treats a firm as a single entity regardless of how the firm is structured. The firm, through its attest services, is now physically entering California and is required to register with the California Board of Accountancy. *The out-of-state CPAs signing the individual (natural person) tax returns on behalf of the firm would now be required to obtain a California Practice Privilege or a California CPA license since the firm has a physical presence in California.*

Former Practice Privilege Handbook at 19-20 (emphases added).

I am pleased to see that these examples have been removed from the Practice Privilege Handbook as of January 26, 2006. The Handbook now merely restates the statutory text. *See* Practice Privilege Handbook at 19, 20.

As set forth below, it appears that an interpretation of Section 5054 that would preclude accountants in registered firms from using that provision would not be the best reading of the statutory text, would not effectuate the Legislature's intent, and would not serve the public policy goals of the Board or the Legislature. An individual accountant who complies with the provisions of Section 5054—provisions that encompass only a relatively small number of accountants—should not be subject to the additional requirement of filing for a California practice privilege or license.

A. Statutory Text

The text of Section 5054 permits "an individual or firm" to engage in this limited form of tax practice, provided that "the individual or firm" meets certain conditions. The structure of the section makes clear that an individual can invoke this provision even if affiliated with a firm. Thus, "an individual" who is licensed and in good standing in another State may prepare tax returns for an individual Californian if "the individual" meets the three conditions, *i.e.*, if he "does not physically enter California," "does not solicit California clients," and "does not assert that the individual . . . is licensed . . . to practice public accountancy in California."

Although the individual accountant in the Practice Privilege Handbook's now-removed examples had met each of these three conditions, the Handbook maintained that "the firm is the entity legally recognized as doing the tax return," Former Practice Privilege Handbook at 19, and that the *accountant* therefore must obtain a practice privilege. The Handbook did not cite any California law establishing this proposition, and even if it is accurate as a general matter, Section 5054 affirmatively provides that an individual accountant "may prepare" tax returns for individuals "[n]otwithstanding any other provision of" the accountancy statutes.

Especially if the return is issued under the individual accountant's name, there should be no doubt that the accountant is entitled to use the limited exception set out in Section 5054. Even if the tax return is issued in the name of the firm, that does not trigger an obligation for the individual CPA to seek a practice privilege. The individual CPA has still complied with all of the conditions of Section 5054, and therefore remains exempt from the requirement to obtain a license or a practice privilege. As for the firm, in the examples it has already registered with the Board, so it has satisfied its own obligations.

The deleted answers in the Practice Privilege Handbook apparently were based on two assumptions: that if the accountant's firm is registered in California, the firm has "physically enter[ed] California to practice public accountancy," and that if the firm has physically entered California, then the individual accountant is also deemed to have entered California. I disagree with these assumptions. First, although a firm that applies for registration certainly submits to the regulatory jurisdiction of the Board, the statute uses the specific term "physically enter California," which appears to require more than just filing for registration. Second, even if the firm has "physically enter[ed]" the State, it does not follow that the individual accountant is also deemed to have entered—and disqualified himself from invoking Section 5054.

As discussed above, the conditions in Section 5054 can apply to "the individual" on his own, without regard to "the firm," thus permitting "the individual" to invoke the section's exception for tax practice.[1]

B. Legislative Intent

What little legislative history is available strongly suggests that the Legislature intended to allow qualifying accountants to engage in limited tax practice pursuant to Section 5054, whether or not they are associated with a registered firm. The floor analyses prepared for both the Senate and the Assembly stated that the new section would allow an accountant to provide tax services to individuals "without a California license, a practice privilege, or a public accounting firm employer registered in California." Senate Floor Analysis at 5; Assembly Floor Analysis at 2. Plainly, therefore, the Legislature intended that an accountant could practice pursuant to Section 5054 without applying for licensure; securing a practice privilege; or establishing a relationship with a registered firm, presumably to fit within the supervised-practice exception of Section 5053.

C. Public Policy

Reading Section 5054 to treat an accountant's association with a registered firm as disqualifying would be not only inconsistent with the Legislature's intent, but also contrary to sound public policy. That approach would treat an out-of-state accountant much less favorably if he works for a registered firm. An out-of-state accountant who does not work for a registered firm can engage in limited tax practice under Section 5054, provided that he meets the three conditions. If he works for an unregistered firm, that status is no obstacle; indeed, the Board does not require that an accountant work for a firm that is registered or licensed *anywhere* in order to invoke Section 5054.

This disparate treatment would be inappropriate. Accountants who work for registered firms belong to institutions that have submitted to the California Board's jurisdiction, satisfied the requirements for registration, and remained in good standing. California-registered firms are also subject to various reporting requirements, pursuant to which they disclose professional discipline, civil judgments related to professional conduct, and government investigations involving their accountants. *See* CAL. BUS. & PROF. CODE § 5063.

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[1] Indeed, the structure of the statute demonstrates that Section 5054 cannot be read to bar "an individual" from engaging in limited tax practice if "the firm" has entered California. If each of the references to "the individual or firm" in Section 5054 were read consistently with that interpretation, the statute would bar "an individual" associated with a registered firm from telling his clients "that the . . .firm is licensed or registered to practice public accountancy in California," even though that information would be both true and valuable. That individuals associated with registered firms cannot logically be barred from invoking Section 5054 without also yielding this absurd result, provides an additional reason not to adopt this strained interpretation of the text.

Section 5054 was designed to *allow* this type of accountant to continue to service clients in California. These accountants should not receive less favorable treatment than accountants who work for unregistered firms. Such an exclusion would cause an unnecessary disruption of the client relationship without improving client service.

D. Recommendation

Accordingly, the Board should make clear that any individual accountant who meets Section 5054's three conditions may engage in the form of limited tax practice described in that statute. If the accountant does not physically enter California, does not solicit California clients, and does not hold himself out as a California licensee, Section 5054 permits him to prepare tax returns for individual Californians, irrespective of whether he is employed by a registered California firm.

III. Application of Practice-Privilege Requirement to Out-of-State Work

I am also concerned by the Practice Privilege Handbook's treatment of other accounting work, such as audits, that occurs entirely outside California. Several of the Q&A illustrations in the Practice Privilege Handbook assert that an accountant must obtain a California practice privilege to service "clients who reside in California," even if no work is actually performed in California. Previously, the Practice Privilege Handbook had used the much more vague formulation "a California client" instead of "clients who reside in California." I strongly support the deletion of the concept of "a California client": that term does not appear in the governing statute or regulations; the Handbook did not define it; and, in fact, the Handbook contained conflicting suggestions as to what might constitute "a California client."

While I applaud the removal of this vague concept and believe that the new formulation of "clients who reside in California" is a step in the right direction, I still have some concerns about the specificity of the new language as well as its basis. I discuss these concerns below.

As revised, the Practice Privilege Handbook states:

> Q: I'm a CPA in another state and do not plan to be in California. I do only one tax return for a California client. Do I need a California practice privilege?
>
> A: Yes, in order to provide public accounting services to *clients who reside in California* you will be required to obtain a California practice privilege or obtain a California CPA license. Preparing tax returns as a CPA is a service that falls within the definition of the practice of public accountancy contained in Section 5051 of the California Accountancy Act.
>
> * * * *

> Q: I'm a CPA in another state. One of my clients retired and moved to California. Do I need a practice privilege to continue to prepare that client's tax return?
>
> A: Yes, in order to provide public accounting services to *clients who reside in California* you will be required to obtain a California practice privilege or obtain a California CPA license. Preparing tax returns as a CPA is a service that falls within the definition of the practice of public accountancy contained in Section 5051 of the California Accountancy Act.
>
> * * * *
>
> Q: I am a Utah CPA who prepares state tax returns filed with the California Franchise Tax Board for my Utah resident clients. Do I need a practice privilege after December 31, 2005?
>
> A: No. However, you would need to obtain a California practice privilege or obtain a California CPA license to practice public accountancy as defined in Section 5051 of the California Accountancy Act if you intend to service *clients who reside in California.*
>
> * * * *

Practice Privilege Handbook at 19-20 (emphases added).

As discussed below, the term "clients who reside in California" is not drawn from the governing statute and is not defined in regulations or other Board guidance. I am concerned that using this vague concept to determine when an out-of-state accountant must file for a practice privilege will cause uncertainty, both about the accountant's duty to seek a privilege and about the Board's statutory and constitutional authority to adopt such a potentially far-reaching rule.

A. Undefined Standard

The Practice Privilege Handbook does not define what determines whether a business "resides in California." Nor do the California accountancy statutes or regulations, which do not use the concept to refer to businesses. (Section 5054 uses the concept to apply only to natural persons.)

Indeed, the Practice Privilege Handbook offers somewhat conflicting indications as to what may constitute a business client that resides in California. In one example, the Handbook suggests that if a client's "primary business operation" is in California but its "administrative office" is not, the accountant need not obtain a California practice privilege unless he "physically enters California to practice public accountancy." Practice Privilege Handbook at 21. It is unclear, however, whether the Practice Privilege Handbook means to establish definitively that a business "resides" only in the State where its "administrative office" is located.

B. Statutory and Constitutional Concerns

The basis for the requirement that an accountant seek licensure or a practice privilege is Section 5050. That section requires an accountant to obtain a practice privilege or a California CPA license only if he seeks to "engage in the practice of public accountancy *in this state*" (emphasis added). Although the statute defines "practice of public accountancy," it does not define "in this state," and thus gives that term its ordinary meaning.

Merely servicing "clients who reside in California" does not in all cases constitute practicing public accountancy "in this state," as that term is ordinarily read or understood. The statute evidently makes the location of the services the critical factor, not the location of the client. The definition of public accountancy includes, for example, "perform[ing]" or "render[ing] professional services to clients for compensation." CAL. BUS. & PROF. CODE § 5051(c), (e). If no service is "perform[ed]" or "render[ed]" in California, then it would appear that the accountant is not practicing public accountancy in California ("in this state") and should not need to obtain a practice privilege or a license.

Were the Board to enforce the practice-privilege requirement as the Practice Privilege Handbook suggests, it would be regulating the conduct of accountants who have no contact with California. Indeed, it would absolutely forbid these accountants from accepting specified engagements under certain circumstances, potentially even if the client's entire business operation were located in another State and the work were performed entirely in that other State. The Federal Constitution limits a State's power to regulate beyond its borders in this fashion. The U.S. Supreme Court has struck down state regulations that seek to "project" the State's own regulatory regime onto businesses in other States. The interpretations suggested in the Handbook implicate and may exceed these constitutional limits. In the face of such serious constitutional questions, the Board should avoid such a broad interpretation, especially as the statutory text supports a far narrower view.

C. Conflict with Other States' Regulation of Accountancy

Requiring a California practice privilege is not necessary to ensure that services provided to California licensees will be regulated. Any accountant who provides services outside California will be regulated by the State of licensure. For the Board to insist that accountants who never enter the State also obtain a practice privilege in California, merely because the client has operations there, would only further complicate the regulatory framework with which accountants must comply.

The National Association of State Boards of Accountancy (NASBA) is in the process of addressing the complexities of multistate regulation, including issues like this one. NASBA and the AICPA have recently promulgated a new version of the Uniform Accountancy Act, Section 23 of which includes a substantial-equivalency provision similar to the practice-privilege legislation that California adopted. The UAA requires the State of licensure to receive and address disciplinary concerns raised by other jurisdictions. *See* UNIF. ACCOUNTANCY ACT § 23(b).

The NASBA committee that drafted the UAA will be meeting over the coming year to draft implementing regulations, which will likely address any potential regulatory conflicts and clarify which State should be primarily responsible for regulating an audit engagement that occurs in multiple places. While this process is ongoing, the Board should not take any steps that disrupt the current system of regulation by the State of licensure and the State where services are rendered. It would be appropriate for the Board to revisit the issue next year, once the new UAA rules have been promulgated and the Board has had a chance to determine whether they adequately address the issue of regulating multistate practice. The next year will also give the Board experience with the operation of the practice privilege in California and allow it to assess how frequently this issue arises.

D. Recommendation

At least for the first year that the new practice privilege is in effect, the Board should enforce the statutory requirement, which requires an accountant to obtain a practice privilege only when the accountant physically enters California to practice public accountancy. The Committee and the Board should not ratify the Handbook's vague concept of a "client who resides in California," which suffers from a lack of clarity and from the potential defects of statutory and constitutional authority identified above. The Board will be able to revisit the issue next year with more information at its disposal, once regulations to implement Section 23 of the revised UAA have been developed.

IV. Applicants from Non-Substantially Equivalent States

Applicants for a practice privilege must demonstrate in one of three ways that they possess credentials that are "substantially equivalent" to a California licensee's: they may show that they were licensed by a state recognized as substantially equivalent; that they have "continually practiced public accountancy . . . for at least four of the last ten years"; or that their individual qualifications are substantially equivalent to California's standards. CAL. BUS. & PROF. CODE § 5096(a). The statute allows the Board to determine how an applicant may demonstrate sufficient individual qualifications. *See id.* § 5096(a)(3), (b). By regulation, the Board has provided that an accountant may have his credentials verified by CredentialNet, which is operated by NASBA. CAL. CODE REGS. tit. 16, § 27(b).

I agree with the Board that approval by CredentialNet should be sufficient to demonstrate the qualifications for a practice privilege. I am concerned, however, about the potential delay in the process caused by CredentialNet. Under the regulations, an accountant must actually "obtain the required substantial equivalency determination" from CredentialNet "[p]rior to seeking a practice privilege." *Id.* One great benefit of the practice-privilege system is the flexibility it allows out-of-state accountants to travel to California on short notice, to notify the Board on a relatively simple and straightforward form that can be submitted electronically, to pay the applicable fee at any time within 30 days, and to begin practicing no later than the time of submission (and up to five days earlier, pursuant to the safe-harbor provision that is in effect for 2006 and 2007, *id.* § 30). The regulations, however, deny this flexibility to an accountant who is licensed by a State that is not recognized as "substantially equivalent" and who does not meet the four-years-in-ten qualification, even if his individual credentials are unquestionably within

California's standards. He may not seek the practice privilege until NASBA has completed his paperwork. If he may not obtain the practice privilege, he may not practice public accountancy in California.

The statute and regulation allow the Board to determine what individual qualifications meet the standard of substantial equivalency; neither the Legislature nor the Board has suggested that the CredentialNet evaluation should be the exclusive means of demonstrating appropriate qualifications. *See* CAL. BUS. & PROF. CODE § 5096(a)(3); CAL. CODE REGS. tit. 16, § 27(b). I note that Section 23(a)(2) of the Uniform Accountancy Act contains a "grandfather clause" allowing the Uniform CPA Examination to substitute for other credentials until the year 2012, by which time those States that are not yet substantially equivalent are expected to have upgraded their requirements to meet that standard.

It would be appropriate for the Board to add the Uniform CPA Examination to § 27 as an alternative measure of qualifications. Indeed, a candidate who has already passed the Uniform CPA Examination has already met the primary qualification for licensure. *See* CAL. BUS. & PROF. CODE §§ 5092(c), 5093(c); CAL. CODE REGS. tit. 16, § 6. NASBA's Uniform Accountancy Act recognizes that a satisfactory test score justifies excusing an applicant from the requirement that he have completed a set number of hours of education, *see* UNIF. ACCOUNTANCY ACT § 23(a)(2). For the same reason, a satisfactory test score justifies excusing an applicant for a practice privilege from rote compliance with the four-years-in-ten requirement.

V. Notification of Routine Renewals

The Board's approved notification form includes a space for the out-of-state accountant to fill in the expiration date of his current accountancy license. This information is not part of the public record, however. *See* Practice Privilege Handbook at 10. Rather, only the State of licensure is made public, *see id.*, so a member of the public seeking to verify that a holder of a California practice privilege is still in good standing in the State of licensure would have to check with that State. Holders of a practice privilege agree to keep the Board informed of any change to the information reported on the notification form within 30 days. CAL. CODE REGS. tit. 16, § 33.

The Practice Privilege Handbook provides:

> If the CPA license identified in the Notification Form used as the basis for qualifying for a California Practice Privilege is renewed during the term of an individual's California Practice Privilege, it must be reported to the Board through your online client account or in writing within 30 days of the renewal date. An individual may be subject to a fine of $250 to $5,000 for failure to comply with this requirement.

Practice Privilege Handbook at 11. Thus, even if the accountant remains in good standing, and the State of licensure and the license number remains unchanged, the Practice Privilege Handbook requires notification even of a routine renewal.

This requirement creates an unnecessary burden on holders of the practice privilege. For an accountant in good standing, renewals are routine events, and in some cases may even be handled primarily by administrative or compliance personnel. The Board would be able at all times to verify the status of any accountant who holds a practice privilege: applicants agree "[t]o respond fully and completely to all inquiries" by the Board and to allow the Board to contact any other state agencies concerning their credentials. And the holder of a privilege, like a licensee, would still be obliged to report to the Board any "refusal to renew a certificate" or other termination of the right to practice by the State of licensure. CAL. BUS. & PROF. CODE §§ 5063(a)(2), 5096.7(a). Finally, as noted above, requiring the licensee to submit regular reports would not benefit California consumers, because the expiration date would not be public information in any event.

Therefore, the Board should refrain from requiring holders of a practice privilege to submit additional notifications each time they renew their licenses in their home States. Rather, licensees should be obliged to notify the Board only if their status as a licensee in good standing changes.

VI. Disqualifying Conditions

The Board has appropriately exercised its authority to clarify the statutory list of disqualifying conditions and to make appropriate *de minimus* exceptions. As the Board has recognized, it is important to make the list of disqualifying conditions as straightforward and easy to comprehend as possible, so that no accountant mistakenly thinks that he is not subject to a disqualifying condition and accordingly attempts to practice pursuant to the privilege without Board approval.

In that spirit, I offer a few additional areas in which further clarification is warranted.

A. Investigations

I recommend clarifying the disqualifying condition relating to pending investigations. In particular, I note that the SEC and PCAOB make a practice of notifying accountants or firms that they are implicated in formal investigations. *See, e.g.*, PCAOB Rule 5101. These agencies sometimes receive complaints against accountants, which are quickly dismissed after preliminary inquiry and without the need for a formal order of investigation. Indeed, in some such instances the subject of the complaint is not formally notified of the inquiry.

The Board should take the position that a pending investigation by the SEC, PCAOB, or other agency that uses the same procedure is a disqualifying condition only if the SEC, PCAOB, or other agency has issued a formal order of investigation that names the accountant seeking or holding the practice privilege. Such a position would be entirely consistent with legislative intent; when the Legislature wants to include preliminary stages of inquiry that occur before a formal investigation, it knows how to do so. *See, e.g.*, CAL. BUS. & PROF. CODE § 5063(b)(3)-(4) (requiring licensees to notify the Board of any formal order of investigation by the SEC *or* of any invitation to make a Wells submission, which occurs before the SEC issues a formal order). No such language appears in Section 5096(g)(2), which sets out the list of disqualifying conditions.

The Board should also amend Section 32(c)(3) of the regulations to clarify that the pendency of an informal inquiry by the PCAOB staff, pursuant to PCAOB Rule 5100, is not a disqualifying condition.

B. Duration of Privilege Following Resolution of Disqualifying Conditions

A practice privilege lasts for one year from its effective date, unless the holder of the privilege files a new notification form or receives a California license. CAL. CODE REGS. tit. 16, § 29(b)-(c). In general, as the Board's regulations recognize, the year should run from the date the notification form is filed, because that is the date that the practice privilege becomes effective.

The Practice Privilege Handbook takes the position that when approval of the practice privilege is delayed because the Board must consider a disqualifying condition, the delay counts against the privilege holder's one year. *See* Practice Privilege Handbook at 17 ("Your California Practice Privilege term still expires one year from the date of submission of the Notification Form and is not extended by a delay in your receiving practice rights.") The Board should clarify Section 29 of the regulations to make plain that the one year runs from the effective date of the privilege even if the privilege is not effective upon the filing of the notification. For example, if an accountant has one of the specified disqualifying conditions and must seek the Board's approval to obtain a practice privilege, the Board may take some time to consider and process his request. During that time, the accountant cannot practice in California. The one-year practice privilege therefore should begin when the accountant receives permission to practice.

Clarifying the regulation and specifying that, when Board approval is required, the one year begins when the Board approves the application, would benefit both accountants and the Board by reducing the need to submit and process duplicative filings. There is no need to impose a shortened renewal deadline on accountants once Board approval is granted; holders of a practice privilege, of course, remain obliged to notify the Board if any new disqualifying condition arises or if any of the information in their applications change. *Id.* §§ 32(b), 33.

C. Renewal of Privilege Following Resolution of Disqualifying Conditions

A practice privilege expires after one year but may be renewed upon submission of a new notification form. There is an ambiguity in the regulations concerning renewals of practice privilege by applicants who previously were the subject of a disqualifying condition, but who were granted a practice privilege by the Board.

For example, suppose that the Board grants a practice privilege to an accountant who was convicted of a petty offense while in college, and who properly disclosed that conviction on his notification form pursuant to Section 32(c)(1) of the regulations. When that accountant applies for a new practice privilege, may he commence practice immediately upon notification, or must he again await Board approval because of his past disqualifying condition?

An appropriate answer can be found in line F of the "Disqualifying Conditions" section of the notification form. That line asks the applicant whether he has previously been notified by the Board "that prior Board approval is required before practice under a new practice privilege may commence."

The Board should adopt a practice, whenever it approves an application for practice privilege by an accountant with a disqualifying condition, of notifying the applicant whether he must seek Board approval before applying again for a practice privilege. In the above example of the past conviction for a petty offense, for instance, it would be appropriate to inform the applicant that he may apply in the future for a practice privilege without Board approval—unless, of course, a new disqualifying condition arises before that time.

This letter is not intended to be an all inclusive list of issues raised by the handbook, the FAQs contained therein or the regulations as interpreted by the forgoing documents.

As I stated at the last board meeting, I appreciate the efforts of the board and its staff to address these very serious issues. I look forward to continuing our discussions at the next board meeting. In the meantime, if I can answer any questions please do not hesitate to contact me.

Sincerely,

Richard Robinson

cc: Carol Sigmann

STATE OF CALIFORNIA

Memorandum

TO:	**Carol Sigmann, Executive Officer** **California Board of Accountancy**	Date:	Feb. 9, 2006
		Tel.:	(916) 574 8243
FROM:	**George P. Ritter** **Staff Counsel, DCA**	Fax:	(916) 574 8623

SUBJ: **Response to Comments Made by Mr. Richard Robinson Concerning § 5054 & the Board's Jurisdiction**

Mr. Richard Robinson has raised several objections to the application of Business and Professions Code Section 5054 and the jurisdiction of the Board. You have asked me to provide a response to the issues he has raised.

1. Section 5054

Section 5054 provides an exemption from licensure and practice privilege for CPAs or public accountancy firms which prepare individual tax returns for natural persons who are California residents. The exemption is applicable as long as the individual CPAs or firms are not physically present in the State of California.

Mr. Robinson's concern with Section 5054 centers on the situation where a CPA who is not licensed in California works for a firm which is registered in this State. He believes that if the CPA that prepared the tax return does not enter California, he or she should qualify for this exemption.

B. & P. Code § 5054 (2005 Stats. Ch. 658) provides that:

> *[A]n individual or firm* holding a valid and current license . . . to practice public accountancy from another state may prepare tax returns for natural persons who are California residents . . . without obtaining a permit to practice public accountancy . . . or a practice privilege . . . provided that *the individual or firm* does not physically enter California . . . .

"*The*" individual or firm which cannot enter California is also the same "individual or firm" which is a candidate for an exemption under Section 5054. Thus, the question becomes: Is that same individual or firm physically present in California?

For an individual, the issue of physical presence is a simple one. For firms, it is not. Firms such as corporations or partnerships do not have an individual's "physical presence." So their physical presence must be measured by the level of their business activities. (*International Shoe v. State of Washington*, 326 U.S. 310, 316 (1945); Corp. Code § 15700). When those activities are "sufficiently substantial and [of a] continuous nature," the corporation or partnership "is treated as if it had a '"physical presence"' in the [state]." (*Serafini v. Superior Ct*, 68 Cal. App. 4th 70, 79 - 80, 80 Cal. Rptr. 2d 159 (1998)).

The standard used to establish physical or economic presence is the same as that for determining whether a firm is subject to the general jurisdiction of the courts of the State. "The standard for establishing general jurisdiction . . . requires that the defendant's contacts be of the sort that approximate physical presence." (*Bancroft & Masters, Inc. v. Augusta National Inc.*, 223 F.3d 1082, 1086 (9th Cir. 2000)). "[E]conomic presence within the state [is] equated with physical presence for jurisdictional purposes." (*Messerschmidt Development Co., Inc. v. Crutcher Resources Corp.*, 84 Cal. App. 3d 819, 824, 149 Cal. Rptr. 35 (1978)). Thus, the standard used by the courts to establish economic or physical presence or general jurisdiction is that the firm's activities are "substantial . . . continuous and systematic." (*Perkins v. Benguet Mining Co.*, 342 U.S. 437, 447 – 448 (1952); *Gates Learjet Corp. v. Jensen*, 743 F.2d 1325, 1331 (9th Cir. 1984)).[1]

Applying these principles, it would appear extremely unlikely that a registered firm conducting the practice of accountancy in California could claim that it was not physically present in this State. For example, when a partnership "engage[s] in the practice of accountancy" in California, it must be registered with the Board. (B. & P. Code § 5072(a)). Registration requires that:

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[1] . Physical presence should be contrasted with minimum contacts in a state *related to a cause of action* brought against an out-of-state defendant. This is known as specific as opposed to general jurisdiction. Under that doctrine, the defendant must "purposefully avails itself of the privilege of conducting activities within the forum State, thus invoking the benefits and protections of its laws." *Hanson v.Denckla*, 357 U.S. 235, 253 (1958). Accordingly, a licensed corporation or partnership could be characterized as one that "purposefully avails itself" of "the privilege of conducting [business] within the forum State" and thus subject to specific, but not necessarily general jurisdiction.

> At least one general partner shall hold a valid permit to practice as a certified public accountant, public accountant, or accountancy corporation, or shall be an applicant for a certificate as a certified public accountant under Sections 5087 and 5088. (B. & P. Code § 5072(b)).

One can thus infer that if a partnership is registered, it is doing business in this State on a continuous basis and acting through at least one general partner who is a California licensed CPA.

Likewise, an accountancy corporation registered with the Board must do so pursuant to the Moscone-Knox Professional Corporation Act . . . . (B. & P. Code § 5150). Under that Act:

> A professional accountancy corporation is one "that is engaged in rendering professional services." (See Corp. Code § 13401(b)).

For a limited liability partnership:

> [A] partnership . . . shall file with the Secretary of State a registration . . . stating the following: (1) The name of the partnership. (2) The address of its principal office. (3) The name and address of the agent for service of process on the limited liability partnership in California. (4) A brief statement of the business in which the partnership engages . . . . (Corp. Code § 16953).

Thus, any accountancy firm which is registered with the Board is probably doing business in California on a "substantial . . . continuous and systematic" basis. If that is the case, it would then be physically present in this State.

Accordingly, a CPA licensed in another state and employed by a firm registered in California would not be able to qualify for an exemption under Section 5054 if he or she prepared a tax return for one of his or her firm's clients who is a California resident. The reason is that the CPA is not acting in his or her individual capacity, but as an agent of the firm. Even though he or she might be absent from California, his or her registered firm is not. Because the firm, not the individual, is the entity legally recognized as doing the tax preparation work, the requirements of 5054 would not be met.

There are obvious exceptions. For example, if the CPA were "moonlighting" and prepared a tax return for a California resident who is not a client of the firm, then the presence of the firm is immaterial. The CPA is now acting in his or her individual capacity rather than as the agent of the firm. As long as the CPA does not physically enter the State, he or she should be able to qualify for the exemption under Section 5054.

Admittedly, the structure of Section 5054 creates some anomalous results as noted by Mr. Robinson in his letter. The CPA who works for a non-registered firm can qualify for the exemption, while his or her counterpart in the registered firm cannot. Likewise, the CPA who prepares the return in his or her individual capacity can qualify. But if the return is prepared under the name of the firm, the exemption will no longer apply.

The Board has no discretion but to apply the law as it currently exists. Thus, these issues should be addressed to the Legislature where possible amendments to Section 5054 could be considered.

2. Jurisdictional Issues

Questions were raised concerning the scope of the Board's jurisdiction as a State regulatory agency. The limit of jurisdiction in California whether exercised through its courts or its regulatory agencies is governed by the Due Process Clause of the Fourteenth Amendment. (See Code Civ. P. § 410.10.) Under that Amendment, the United States Supreme Court has created what is known as the minimum contacts rule. (*International Shoe v. State of Washington*, 326 U.S. 310 (1945).) "The application of that rule will vary with the quality and nature of the defendant's activity, but it is essential in each case that there be some act by which the defendant purposefully avails itself of the privilege of conducting activities within the forum State, thus invoking the benefits and protections of its laws." (*Hanson v. Denckla*, 357 U.S. 235, 253 (1958).)

It is not necessary that a person physically enter the forum state. The Ninth Circuit case of *Bancroft & Masters, Inc. v. Augusta National Inc.*, 223 F.3d 1082 (9th Cir. 2000) illustrates a recent example of how the minimum contacts doctrine is applied. Bancroft & Masters was a California corporation that sold computer products in the

Bay Area. It had a registered internet name of "masters.com." Registration was done through a third party in Virginia known as NSI. In 1997, the Augusta National Golf Club sent a letter to NSI in Virginia challenging Bancroft & Masters' use of "masters.com." Bancroft & Masters then sued Augusta National in the Federal District Court of Northern California. The Ninth Circuit determined that even though the letter had been sent to Virginia instead of California, there were sufficient contacts to establish jurisdiction. The sending of this letter subjected Augusta National to jurisdiction under what has been termed the "express aiming" doctrine.

> Express aiming is . . . . satisfied when the defendant is alleged to have engaged in wrongful conduct targeted at a plaintiff whom the defendant knows to be a resident of the forum state. (223 F.3d at 1087).

Even though Augusta National had no direct contact with California, its "'intentional . . . actions were expressly aimed'" at that State. (223 F.3d at 1087). Thus, *Bancroft & Masters v. Augusta National Golf Club* stands for the proposition that contact with a forum state, even if on an indirect basis, may be sufficient to establish jurisdiction over a person if he or she purposefully aimed or intended that his conduct have an impact on that state.

Courts have also developed more specific jurisdictional principles for those who render professional services across state lines. For example, in *Clark v. Noyes*, 871 S.W. 2d 508 (Tex. App. 1994), Clark, a resident of Texas, traveled to Cincinnati, Ohio to consult with Dr. Noyes about his injured knee. Dr. Noyes performed surgery in Cincinnati. Clark later filed a medical malpractice action in Texas. The trial court dismissed the case for lack of jurisdiction. The Texas Court of Appeals affirmed.

In holding that there were insufficient minimum contacts with the State of Texas, the Court went through a very thorough discussion of controlling case law including the seminal Ninth Circuit case of *Wright v. Yackley*, 459 F.2d 287 (9th Cir. 1972). It noted that:

> Wright, an Idaho resident, brought suit against a doctor, a South Dakota resident, in federal district court in Idaho for injuries allegedly received from medication prescribed by the doctor. The doctor prescribed the medication in South Dakota while Write was a resident of South Dakota. Wright subsequently moved to Idaho, where she continued to have the prescription

> filled. The doctor's contact with Idaho involved his sending copies of the original prescription to Wright so that the Idaho pharmacist would continue to prescribe the medication. . . . .
>
> . . . . In [affirming dismissal of the case for want of jurisdiction, the Ninth Circuit] noted that all of the acts of which Wright complained occurred in South Dakota. [Citation.] By mailing copies of the existing prescription to Idaho, the doctor did not diagnose or treat Wright. [Citation.] The Ninth Circuit stated that in cases involving personal services, ***the focus should be on where the services were rendered.*** [Citation.] The very nature of medical services is such that their consequences would be felt where the patient went. (871 S.W. 2d at 514 [Emphasis added] [Citations omitted]).[2]

In *Wright* the Ninth Circuit noted that it would have been inclined to find jurisdiction if the doctor "could be said to have treated the patient by mail or have provided a new prescription or diagnosis in such fashion. *In that event, the forum state's interest in deterring interstate medical practice would surely be great.*" (459 F.2d at 289 n. 4). (emphasis added).

This language from *Wright* was relied upon by the Tenth Circuit in *Kennedy v. Freeman*, 919 F.2d 126 (10th Cir. 1990). There, a Texas physician had allegedly misdiagnosed a mole on the thigh of an Oklahoma resident. The Tenth Circuit, in finding personal jurisdiction in Oklahoma discussed the physicians contacts in Oklahoma. Those contacts included the Texas doctor having willingly accepted for analysis in Texas a mole removed by the Oklahoma physician from his Oklahoma patient, the Texas doctor having signed the diagnosis and provided it to the Oklahoma patient through the mail and the Texas doctor having billed the Oklahoma patient for the services.

It is clear from the case law that a patient can not simply travel to obtain medical treatment in another state and expect to be able to sue the physician in the patient's

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[2] . In this respect, the Ninth Circuit also observed in *Wright v. Yackley* that:

> The contact between the doctor and the forum state was based on the appellant's seeking treatment from the doctor while in the doctor's home state. *The nature of the average doctor's localized practice showed no systematic and continuous effort to provide services which were to be felt in foreign states. The residence of the patient was irrelevant and incidental to the treatment provided by the doctor in his home state. The doctor did not purposefully avail himself of the privilege of conducting activities in the forum state.* (459 F.2d at 290 – 91 [Emphasis added].)

home state. However, if the physician provides further services such as follow-up consultations or prescriptions over the phone, through the mail or using the internet directed to the patient in the patients home state, then the home state can establish personal jurisdiction over the physician. Furthermore the same type of analysis is applied to evaluate jurisdiction over other professionals including accountants and auditors.

For example, in *Faleck v. Margolies, Ltd.v. Patrusky, Mintz & Smell* (S.D.N.Y. 1990) U.S.Dist. LEXIS 14624, the Court found that a Canadian chartered accountant who went to New York twice annually to inspect, but not supervise, the inventory of a subsidiary of a Canadian company performed by a New York CPA firm, had purposefully availed himself of the benefits and protections of New York law and was thus subject to jurisdiction. What the Court found to be significant was the fact that the accountant was paid by the parent Canadian company and was performing professional services on behalf of that company in the forum State of New York.

In conclusion, the Board can regulate any acts which are the practice of public accountancy whether they are undertaken by an out-of-state licensee who physically enters the state or who enters the state through mail, telephone, the internet or other means. The only limitation is that the out of state licensee must take some action to direct his or her activities into the state such that it can be said the accountant has purposefully availed himself or herself with the benefits of doing business in California.

State of California
Department of Consumer Affairs

California Board of Accountancy
2000 Evergreen Street, Suite 250
Sacramento, CA 95815-3832

Memorandum

CPC Agenda Item III.A.B.C.
February, 22 2006

To : CPC Members

Date: February 15, 2006

Telephone : (916) 561-1788
Facsimile : (916) 263-3674
E-mail: awong@cba.ca.gov

From : Aronna Wong
Legislation/Regulations Coordinator

Subject : Significant Issues Related to Temporary Practice and/or the Implementation of Practice Privilege

Attached for your consideration is the February 6, 2006, letter from Bruce C. Allen, Director, Government Relations, for the California Society of Certified Public Accountants (CalCPA).

Attachment

February 6, 2006

Ronald Blanc, Esq., President
California Board of Accountancy
2000 Evergreen Street, Suite 250
Sacramento, CA 95815

Dear President Blanc and Members:

The rationale provided for development of California's practice privilege statute was to accommodate the need for expedited movement of partners to comply with Sarbanes-Oxley's requirements for audit partner rotation and to respond to a Government Accountability Office study that found the need to comply with different licensing requirements in different states makes it more difficult for smaller firms to compete with the very largest firms. The Board's UAA Task Force and later the Practice Privilege Task Force attempted to "see if an approach to cross-border practice can be developed that is consistent with the Board's consumer protection mission." *Page 2 of the UAA Task Force's December 17, 2003 minutes*. The goals were ease of entry and consumer protection.

CalCPA participated in the deliberations on practice privilege and supported the legislation in the hope that through the regulatory process reasonable accommodations could be made to protect the public interest while facilitating the cross-border accounting practices. However, we now believe that implementation issues, misunderstandings and the impact of unintended consequences require immediate action to rectify what has become an untenable situation for California taxpayers, the entire CPA profession and its foreign counterparts. To this end we ask your support of AB 1868.

It should be remembered that the goals were ease of practice across state lines and increased consumer protection, but California's attempted implementation of practice privilege has in fact made practice across state lines more difficult. If services are provided by the firm (and most engagements are with a firm), the CBA is requiring the firm to register as a firm with the California Board of Accountancy. Firm registration requires that at least one partner be fully licensed in California. Further, if the firm is a corporation or an LLP, the firm must also register with the Secretary of State. The entire process is costly and time consuming.

In the attempt to streamline the process, accommodate ease of entry, and increase consumer protection, we have come full circle. Now in addition to requiring full licensure and registration for the provision of audit services which was the previous Board policy, the CBA is imposing full licensure and registration for all services.

Full disclosure demands that you be aware of the cost that is being imposed on California

taxpayers who choose to use the services of an out-of-state CPA firm practicing as a professional corporation or a limited liability partnership.

Registration with Secretary of State-	$100 minimum 5 days
Registration with the Franchise Tax Board	$800 (minimum) (unknown Processing time)
California Ethics Exam	$125 for instant grading
Filing application for CA CPA license	$395(unknown processing time)
Firm Registration	$350 (unknown processing time)
Practice privilege for any other CPAs in firm Providing service to California clients	$100 each
Minimum total cost	$1,810

Taxpayers using CPA partnerships will experience a minimum increase of $870.00 due to the licensing/registration fees.

Until the entire application process is completed, a firm may not provide any services to a California client. Business tax returns are due March 15. It is unlikely that a firm could comply with the firm registration requirements even if it wanted to, given the time that it takes the California Board of Accountancy to process applications. Registration is required whether or not the CPA actually enters California. This is unacceptable as a matter of public policy especially since there was no evidence that consumer protection was lacking prior to the creation of the practice privilege.

CPAs providing tax services to California taxpayers are already regulated by the Internal Revenue Service, the Franchise Tax Board and the licensing board of accountancy in their home state. Insertion of the California Board of Accountancy in this scheme becomes over regulation. This issue has been raised in the past and the CBA and the California State Legislature chose to exempt out-of- state CPAs providing tax services to individuals, and Business and Professions Section 5040 was enacted. There is little difference between preparing a business tax return and a personal tax return. Allowing the preparation of personal returns without registration while at the same time requiring registration for business tax returns demonstrates a flawed approach.

A September 27, 2004 memo from Aronna Granick *(now Wong)* indicated that there were three circumstances as approved by the Practice Privilege Task Force and the CBA when an out-of-state CPA would need to seek a California license rather than a practice privilege in order to practice in California:

1) The individual wants to establish his or her principal place of business in California [Business and Professions Code Section 5096(a)]
2) The individual wants to provide services from an office in this state and is not an employee of a California registered firm [Business and Professions Code Section 5096(e)(3).]
3) The individual is the subject of a pending investigation in which the outcome is not likely to be known for some time. This reflects the action of the Practice Privilege Task Force at its meeting of September 9, 2004, based on a recommendation of Gregory Newington, Enforcement Division Chief.

Perhaps it is unintentional, but now anytime a CPA from a non-registered firm provides services to anyone even remotely connected to California, full licensure of at least one partner and firm registration is required.

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The complexity, breadth of reach, inadvertent interference in existing long term client relationships, interference with interstate commerce and artificial impediment to foreign investment are not worth whatever incremental improvement, if any, is achieved in consumer protection.

There is also tremendous confusion with the application of the new law. During previous deliberations and discussions a question was asked about the requirement of a practice privilege permit for litigation support services and expert witness testimony. See September 9, 2004 Enforcement Program Oversight Committee minutes on page 148, where it was reported that expert witness testimony was not considered the practice of public accountancy. However, on Thursday, January 12, 2006, we were informed by CBA staff that litigation support services are indeed considered within the definition of the practice of public accountancy and a practice privilege would be required.

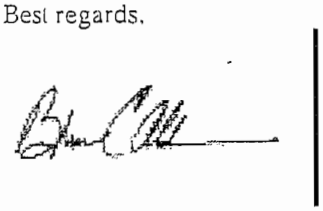
This is an untenable situation for California taxpayers, especially those with multi-state operations. If other states enacted similar provisions, the business owner could be required to retain multiple CPAs to file state tax returns. We agreed that the previous Board policy that required persons and firms providing attest services for California based clients obtain full California licensure needed to be appropriately disclosed and adopted by statute or regulation. We also agreed that a method other than full licensure should be considered for ease of practice. The result even for CPAs providing attest services in California has not eased interstate or international commerce and needs to be immediately corrected.

CPAs across the nation are striving valiantly to comply with the requirements, statutes and interpretations of 54 jurisdictions that do not even agree on what constitutes the practice of public accountancy or what constitutes "Holding Out." We are receiving inquiries from CPAs and organizations throughout the nation raising the issues of constitutionality and impediment to interstate commerce. Additionally, California CPAs are expressing grave concerns as to possible retaliatory action by state boards of accountancy in response to the burdensome California requirements.

California needs to rethink its current approach and act immediately to clean up this confusion. We want to work with the CBA to maintain public protection, but not bar legitimate services being provided to California taxpayers and businesses which operate on an interstate basis and need the professional services of certified public accountants.

It is our hope that the agenda for the February 22nd and 23rd meetings will allow for thorough consideration of all issues related to California's implementation of Section 23. It is our hope that a quick resolution of these issues can be achieved and we can mutually support AB 1868 to provide immediate relief to California taxpayers and the profession.

Best regards,



BRUCE C. ALLEN, Director
Government Relations

cc: CalCPA Government Relations Committee
Carol Sigmann, Executive Officer

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State of California
Department of Consumer Affairs

California Board of Accountancy
2000 Evergreen Street, Suite 250
Sacramento, CA 95815-3832

Memorandum

CPC Agenda Item III.A.B.C.
February 22, 2006

To : CPC Members
Board Members

Date: February, 21, 2006

Telephone : (916) 561-1788
Facsimile : (916) 263-3674
E-mail: awong@cba.ca.gov

From : Aronna Wong
Legislation/Regulations Coordinator

Subject : Comment Letter From the AICPA

Attached for your consideration is a February 15, 2006, letter to Ronald Blanc from Leslie Murphy, CPA, Chairman, AICPA Board of Directors and Barry C. Melancon, CPA, President & CEO, AICPA, communicating their concern regarding the implementation of the Practice Privilege Program (Attachment 1). Also attached for reference are Sections 7 and 23 excerpted from the Uniform Accountancy Act, (UAA), 4th edition, December 2005 (Attachment 2). The AICPA letter notes that the new Practice Privilege requirements, coupled with other provisions within California law, are creating unintended difficulties for the mobility of out-of state CPAs and their firms.

The AICPA letter suggests that departure from UAA Section 23 may be the cause of the difficulty with the Practice Privilege Program, and recommends that the Board give further consideration to the UAA. Board members may recall that the Practice Privilege statutes and regulations were developed by the UAA Task Force (later re-named the Practice Privilege Task Force) as a way of implementing Section 23 of the UAA in California. A CalCPA representative was part of the Task Force and other representatives of the profession participated actively at all Task Force meetings.

In many respects, the Practice Privilege Program the Task Force developed is consistent with Section 23 of the UAA. It allows CPAs from substantially equivalent states to practice in California upon giving notification to the Board. It permits quick, easy on-line notification. In addition, the program expands cross-border practice beyond the limits in the UAA by permitting practice by out-of-state CPAs from states that are not substantially equivalent provided the CPA has practiced public accountancy for four of the last ten years.

The Practice Privilege Program diverges from the UAA in that – consistent with the Board's consumer protection mission – it requires individual notification for practice privilege and contains much more detailed, specific provisions for the suspension or discipline of the practice privilege. These more detailed provisions were deemed necessary to protect consumers because it was unclear how the relevant provisions of the UAA (subsection (a)(3)(c) and subsection (b) of Section 23) would operate in

a real-world regulatory environment. Specific to Section 23(b) some states have laws that preclude boards from taking discipline for acts occurring outside the states' physical boundaries. This Board's Practice Privilege Program also diverges from the UAA in that it provides for a fee so that California CPAs do not need to fund any program costs. However, these divergences are not the source of the current difficulty which relates more to problems associated with firm registration than to cross-border practice by individuals.

The current edition of the UAA speaks to cross-border practice by firms in Section 7(j) which authorizes a non-registered firm to provide services through individuals who meet the requirements of Section 23. Section 7(j) provides for jurisdiction over firms in a manner similar to the way Section 23 provides for jurisdiction over individuals (see Attachment 2). The Board provided comments on this and other provisions in response to the August 1, 2005, UAA Exposure Draft. A copy of the Board's comment letter is provided as Attachment 3. As options for addressing current difficulties are evaluated, the CPC and the Board may want to give Section 7 further consideration.

Attachments

February 15, 2006

Ronald Blanc, Esq., President
California Board of Accountancy
2000 Evergreen Street, Suite 250
Sacramento, CA 95815-3832

Dear President Blanc and Members:

On behalf of the more than 340,000 members of the American Institute of CPAs (AICPA) we would like to take this opportunity to express our concerns to the California Board of Accountancy on the new Practice Privilege regulations and related registration requirements for out-of-state CPAs effective January 1, 2006.

We recognize that the California Board of Accountancy's intent in developing the Practice Privilege requirement was two-fold; the goals were to enhance consumer protection of Californians while allowing for greater mobility for out-of-state CPAs who provide services in California. The AICPA wholly supports both of these objectives, however, the volume of calls we have received from our members throughout the country expressing concern about the burden created by the new requirement and informing us of issues they have encountered that are complicating their efforts to comply have led us to question the effectiveness of the California approach to mobility.

As we examine the Practice Privilege requirement from a national perspective, we are particularly concerned that this approach is a significant departure from the regulatory framework developed jointly by the AICPA with National Association of State Boards of Accountancy (NASBA) to allow CPAs to practice across jurisdictions more easily. Section 23 of The Uniform Accountancy Act (UAA) defines the concept of substantial equivalency, which eliminates the requirement for individual CPAs who practice across state lines to obtain an additional reciprocal or temporary license if they hold a valid license from another substantially equivalent state. California's Practice Privilege requirement deviates from the intent of substantial equivalency by requiring licensees from substantially equivalent states to obtain a Practice Privilege Permit from California. While other states are working to eliminate barriers for CPAs in their states by adopting the UAA concept of substantial equivalency, California's approach is contradicting this concept by putting a new and additional barrier in place.

The implementation of California's new requirement coupled with other provisions within the California law are creating new and unintended difficulties for mobility for out-of-state CPAs and their firms by subjecting them to requirements that they would not otherwise encounter. For example, firms that provide services are required to register with the California Board of Accountancy, and if a firm is a corporation or an LLP, the firm must also register with the Secretary of State and Franchise Tax Board. Firm registration also triggers the requirement that at least one partner be fully licensed in California. We believe that in many instances, especially where business tax preparation is involved, this is a burdensome and unnecessary requirement.

The AICPA will send a representative to the meetings of the Committee on Professional Conduct and the California Board of Accountancy on February 22-23, 2006 and will be available to discuss the national impact of the Practice Privilege requirement and any questions the Board may have about the impact on out-of-state licensees. We appreciate your consideration of our concerns and urge you to consider implementing regulations that more closely mirror the UAA concept of substantial equivalency.

Sincerely,

Leslie Murphy, CPA
Chairman, AICPA Board of Directors

Barry C. Melancon, CPA
President & CEO, AICPA

CC: State CPA Societies
David Costello, President, NASBA
Diane Rubin, Chair, NASBA

SECTION 7
FIRM PERMITS TO PRACTICE, ATTEST AND COMPILATION COMPETENCY AND PEER REVIEW

(a) The Board shall grant or renew permits to practice as a CPA firm to entities that make application and demonstrate their qualifications therefor in accordance with the following subsections of this Section or to CPA firms originally licensed in another state that establish an office in this state. A firm must hold a permit issued under this Section in order to provide attest services as defined or to use the title "CPAs" or "CPA firm".

COMMENT: This Uniform Act departs from the pattern of some accountancy laws now in effect in eliminating any separate requirement for the registration of firms and of offices. The information-gathering and other functions accomplished by such registration should be equally easily accomplished as part of the process of issuing firm permits under this section. The difference is, again, one of form more than of substance but one that should be kept in mind if consideration is given to fitting the permit provisions of this Uniform Act into an existing law.

As pointed out in the comment following section 3(g), above, because a firm is defined to include a sole proprietorship, the permits contemplated by this section would be required of sole practitioners as well as larger practice entities. To avoid unnecessary duplication of paperwork, a Board could, if it deemed appropriate, offer a joint application form for certificates and sole practitioner firm permits.

This provision also makes it clear that unlicensed firms may not provide attest services as defined, or call themselves CPA firms. Certified Public Accountants are not required to offer services to the public, other than attest services, through a CPA firm. CPAs may offer non-attest services through any type of entity they choose and there are no requirements in terms of a certain percentage of CPA ownership for these types of entities as long as they do not call themselves a "CPA firm" or use the term "CPA" in association with the entity's name. These non-CPA firms are not required to be licensed by the State Board.

(b) Permits shall be initially issued and renewed for periods of not more than three years but in any event expiring on [specified date] following issuance or renewal. Applications for permits shall be made in such form, and in the case of applications for renewal, between such dates as the Board may by rule specify, and the Board shall grant or deny any such application no later than _____ days after the application is filed in proper form. In any case where the applicant seeks the opportunity to show that issuance or renewal of a permit was mistakenly denied or where the Board is not able to determine whether it should be granted or denied, the Board may issue to the applicant a provisional permit, which shall expire ninety days after its issuance or when the Board determines whether or not to issue or renew the permit for which application was made, whichever shall first occur.

COMMENT: See the comment following section 6(b) regarding the renewal period.

(c) **An applicant for initial issuance or renewal of a permit to practice under this Section shall be required to show that:**

(1) Notwithstanding any other provision of law, a simple majority of the ownership of the firm, in terms of financial interests and voting rights of all partners, officers, shareholders, members or managers, belongs to holders of a certificate who are licensed in some state, and such partners, officers, shareholders, members or managers, whose principal place of business is in this state, and who perform professional services in this state hold a valid certificate issued under Section 6 of this Act or the corresponding provision of prior law or are public accountants registered under Section 8 of this Act. Although firms may include non-licensee owners the firm and its ownership must comply with rules promulgated by the Board. For firms of public accountants, at least a simple majority of the ownership of the firm, in terms of financial interests and voting rights, must belong to holders of registrations under Section 8 of this Act.

COMMENT: The limitation of the requirement of certificates to partners, officers, shareholders, members and managers who have their principal place of business in the state is intended to allow some latitude for occasional visits and limited assignments within the state of firm personnel who are based elsewhere. In addition, the requirement allows for non-licensee ownership of licensed firms.

(2) Any CPA or PA firm as defined in this Act may include non-licensee owners provided that:

(A) The firm designates a licensee of this state, who is responsible for the proper registration of the firm and identifies that individual to the Board.

(B) All non-licensee owners are active individual participants in the CPA or PA firm or affiliated entities.

(C) The firm complies with such other requirements as the board may impose by rule.

(3) Any individual licensee who is responsible for supervising attest or compilation services and signs or authorizes someone to sign the accountant's report on the financial statements on behalf of the firm, shall meet the competency requirements set out in the professional standards for such services.

(4) Any individual licensee who signs or authorizes someone to sign the accountants' report on the financial statements on behalf of the firm shall meet the competency requirement of the prior subsection.

COMMENT: Because of the greater sensitivity of attest and compilation services, professional standards should set out an appropriate competency requirement for those who supervise them and sign attest or compilation reports.

(d) An applicant for initial issuance or renewal of a permit to practice under this Section shall be required to register each office of the firm within this State with the Board and to show that all attest and compilation services as defined herein rendered in this state are under the charge of a person holding a valid certificate issued under Section 6 of this Act or the corresponding provision of prior law or some other state.

(e) The Board shall charge a fee for each application for initial issuance or renewal of a permit under this Section in an amount prescribed by the Board by rule.

(f) An applicant for initial issuance or renewal of permits under this Section shall in their application list all states in which they have applied for or hold permits as CPA firms and list any past denial, revocation or suspension of a permit by any other state, and each holder of or applicant for a permit under this Section shall notify the Board in writing, within 30 days after its occurrence, of any change in the identities of partners, officers, shareholders, members or managers whose principal place of business is in this State, any change in the number or location of offices within this State, any change in the identity of the persons in charge of such offices, and any issuance, denial, revocation, or suspension of a permit by any other state.

(g) Firms which fall out of compliance with the provisions of the section due to changes in firm ownership or personnel, after receiving or renewing a permit, shall take corrective action to bring the firm back into compliance as quickly as possible. The State Board may grant a reasonable period of time for a firm to take such corrective action. Failure to bring the firm back into compliance within a reasonable period as defined by the Board will result in the suspension or revocation of the firm permit.

(h) The Board shall by rule require as a condition to renewal of permits under this Section, that applicants undergo, no more frequently than once every three years, peer reviews conducted in such manner as the Board shall specify, and such review shall include a verification that individuals in the firm who are responsible for supervising attest and compilation services and sign or authorize someone to sign the accountant's report on the financial statements on behalf of the firm meet the competency requirements set out in the professional standards for such services, provided that any such rule --

(1) shall be promulgated reasonably in advance of the time when it first becomes effective;

(2) shall include reasonable provision for compliance by an applicant showing that it has, within the preceding three years, undergone a peer review that is a satisfactory equivalent to peer review generally required pursuant to this subsection (h);

(3) shall require, with respect to any organization administering peer review programs contemplated by paragraph (2), that it be subject to evaluations by the Board or its designee, to periodically assess the effectiveness of the peer

review program under its charge, and

(4) *may require that organizations administering peer review programs provide to the Board information as the Board designates by rule; and

(5) *shall require with respect to peer reviews contemplated by paragraph (2) that licensees timely remit such peer review documents as specified by Board Rule or upon Board request and that such documents be maintained by the Board in a manner consistent with Section 4(j) of this Act.

*** Due to its 1988 commitment to its members, the AICPA cannot support this provision at this time.**

COMMENT: The AICPA and NASBA both agree that periodic peer reviews are an important means of maintaining the general quality of professional practice.

In the interests of providing flexibility where appropriate or desirable, this provision would give the Board latitude when to require reviews. Paragraph (2) is intended to recognize that there are other valid reasons besides state regulation for which firms may undergo peer reviews (for example, as a condition to membership in the AICPA). It is also intended to avoid unnecessary duplication of such reviews, by providing for the acceptance of peer reviews performed by other groups or organizations whose work could be relied on by the Board. If a peer review requirement is established by the Board, paragraph (3) requires that the Board assure that there is an evaluation of the administration of the peer review program(s) which is accepted by the Board, which is performed either by the Board or its designee. Paragraph (4) would require the administering entities of peer review programs to provide the Board information, as required by rule. Paragraph (5) requires that licensees remit peer review documents to the Board, as specified by rule, and that these documents would be maintained subject to the confidentiality provision in Section 4(j) of the Act.

Paragraphs (4) and (5) primarily address the ability of the Board to have direct access to peer review results. Previous editions of the UAA contained language that could have been interpreted to either not permit or to limit state boards' access to results of the peer review process. Language that restricted the Board's ability to access the results of peer review was consistent with the AICPA's commitment to its membership to maintain the confidentiality of peer review materials that were generated through the AICPA peer review program. However, in response to regulatory concerns it was determined that new language was needed to provide for greater transparency. At its spring 2004 meeting, AICPA's governing Council approved a resolution in support of increased transparency in the peer review process. However, as a result of the AICPA's 1988 commitment to its membership to maintain the confidentiality of peer review results, the AICPA's Council will not act on its resolution without a vote of the AICPA's membership. The AICPA will not pursue a vote of its membership until the membership has fully considered the issues surrounding this matter. Until that time, a solution for the UAA was crafted that recognized the authority of state boards of accountancy to take action and at the same time allowed the Institute to keep its commitment to the AICPA membership on confidentiality of peer review materials. For that reason, paragraphs (4) and (5) are marked with an asterisk (*) that states "Due to its 1988 commitment to its members, the AICPA cannot support this

provision at this time."

The term "peer review" is defined in section 3(n).

(i)(1) **Any CPA firm with a permit in this state may perform services through its individuals licensed in another state whose principal places of business are not in this state and who meet the requirements in Section 23 of this Act. However, the CPA firm:**

(A) Shall provide name(s) of such individuals to the Board of Accountancy upon request

(B) Shall, by utilizing the privileges granted under this provision, consent on its own behalf and for the individual licensees to:

(i) cooperate in any Board investigation regarding any of the individual licensees of the CPA firm even if the individual is no longer an owner or employed by the CPA firm;

(ii) accept service of process from the Board on its own behalf and for the licensees;

(iii) be subject to the administrative jurisdiction of the state board regarding enforcement matters arising out of or pertaining to the use of the practice privileges provided under this subsection; and

(iv) comply with the state's accountancy laws and rules while using practice privileges under this subsection.

(2) An individual licensee whose CPA firm has complied with the preceding subsection shall not be required to file the notice required under Section 23 of this Act only as long as said individual licensee remains an employee or owner of the CPA firm.

(j) **A CPA firm with a permit in another state which does not have an office in this state may provide professional services in this state through individuals that meet the requirements set out in Section 23 and such individuals shall be exempt from the notice requirement set out in Section 23 if the CPA firm:**

(1) has filed a master notice, which shall be renewed not more frequently than annually, to all participating substantially equivalent jurisdictions, including this Board, by giving notice to the NASBA Qualifications Appraisal Board (or other comparable service designated by the Board); provided the information as maintained by NASBA (or such other comparable service) is accessible to this Board and includes the address of the firm and the name of the individual licensee responsible for filing the master notice.

(2) maintains a system of records reasonably designed to record for each calendar

year the name, certificate number, state of licensure and principal place of business of each individual licensee who has used practice privileges in this state pursuant to Section 23 of this Act.

(3) has affirmed in its master notice that it consents in its own behalf and for the individual licensees to the requirements set forth in Section 7(i)(1)(B).

COMMENT: Sections 7(i) and 7(j) enhance substantial equivalency by adding new options for firms and for their substantially equivalent personnel. The procedure available under these Sections, makes substantial equivalency available on a "firm-wide" basis. However, Section 23 is still available should the firm prefer that its personnel file individual notices under that section. The provisions also preserve the enforcement provisions found in Section 23, which are designed to protect the public.

Under Section 7(i), a firm that has a permit in a state may offer services through substantially equivalent CPA personnel who are licensed in other states. These individuals may exercise practice privileges in the state on behalf of a CPA firm, without individually notifying the board. In addition, the CPA firm holding a permit in the state is not required to file a notice for the individual CPAs; it need only provide information to the board of accountancy upon request. However, the firm would be required to keep track of these individuals and submit their names to the board upon request. The firm must also cooperate in board investigations of the individuals, accept process of service for the licensees, and consent on behalf of the individual to be under the state's administrative jurisdiction and to comply with the state's laws and rules.

Under Section 7(j), a CPA firm that does not have a permit in the state may file a master notice with NASBA's Qualification Appraisal Board or another comparable service designated by the board of accountancy. If the CPA firm complies with the requirements of Section 7(j), the CPA firm's substantially equivalent CPAs are exempt from the state-by-state notification requirement set out in Section 23.

SECTION 23
SUBSTANTIAL EQUIVALENCY

(a)(1) **An individual whose principal place of business is not in this state having a valid certificate or license as a Certified Public Accountant from any state which the NASBA National Qualification Appraisal Service has verified to be in substantial equivalence with the CPA licensure requirements of the AICPA/NASBA Uniform Accountancy Act shall be presumed to have qualifications substantially equivalent to this state's requirements and shall have all the privileges of certificate holders and licensees of this state without the need to obtain a certificate or permit under Sections 6 or 7. However, such individuals shall notify the Board of their intent to enter the state under this provision.**

(2) **An individual whose principal place of business is not in this state having a valid certificate or license as a Certified Public Accountant from any state which the NASBA National Qualification Appraisal Service has not verified to be in substantial equivalence with the CPA licensure requirements of the AICPA/NASBA Uniform Accountancy Act shall be presumed to have qualifications substantially equivalent to this state's requirements and shall have all the privileges of certificate holders and licensees of this state without the need to obtain a certificate or permit under Sections 6 or 7 if such individual obtains from the NASBA National Qualification Appraisal Service verification that such individual's CPA qualifications are substantially equivalent to the CPA licensure requirements of the AICPA/NASBA Uniform Accountancy Act. However, such individuals shall notify the Board of their intent to enter the state under this provision. Any individual who passed the Uniform CPA Examination and holds a valid license issued by any other state prior to January 1, 2012 may be exempt from the education requirement in Section 5(c)(2) for purposes of this Section 23 (a)(2).**

(3) **Any licensee of another state exercising the privilege afforded under this section hereby consents, as a condition of the grant of this privilege:**

(a) **to the personal and subject matter jurisdiction and disciplinary authority of the Board,**

(b) **to comply with this Act and the Board's rules; and,**

(c) **to the appointment of the State Board which issued their license as their agent upon whom process may be served in any action or proceeding by this Board against the licensee.**

COMMENT: Subsection 23(a)(3) is intended to allow state boards to discipline licensees from other states that practice in their state. Under Section 23(a), State Boards could utilize the NASBA National Qualification Appraisal Service for determining whether another state's certification criteria are "substantially equivalent" to the national standard outlined in the AICPA/NASBA Uniform Accountancy Act. If a state is determined to be "substantially equivalent," then individuals from that state would have ease of practice rights in other states.

Individuals who personally meet the substantial equivalency standard may also apply to the National Qualification Appraisal Service if the state in which they are licensed is not substantially equivalent to the UAA.

Individual CPAs who practice across state lines or who service clients in another state via electronic technology, would not be required to obtain a reciprocal certificate or license if their state of original certification is deemed substantially equivalent, or if they are individually deemed substantially equivalent. Under Section 23, the CPA merely must notify the Board of the state in which the service is being performed. However, licensure is required in the state where the CPA has their principal place of business. If a CPA relocates to another state and establishes their principal place of business in that state then they would be required to obtain a certificate in that state. See Section 6(c)(2). Likewise, if a firm opens an office in a state they would be required to obtain a license in that state. See also Sections 7(i) and 7(j) which allow the use of substantial equivalency on a firm wide basis.

As it relates to the notification requirement, states should consider the need for such a requirement since the nature of an enforcement complaint would in any event require the identification of the CPA, and a CPA practicing on the basis of substantial equivalency will be subject to enforcement action in any state under Section 23 (a)(3) regardless of a notification requirement.

Implementation of the "substantial equivalency" standard and creation of the National Qualification Appraisal Service will make a significant improvement in the current regulatory system and assist in accomplishing the goal of portability of the CPA title and mobility of CPAs across state lines.

In order to be deemed substantially equivalent under Section 23(a)(1), a state must adopt the 150-hour education requirement established in Section 5(c)(2). A few states have not yet implemented the education provision. In order to allow a reasonable transition period, Section 23(a)(2) provides that an individual who has passed the Uniform CPA examination and holds an active license from a state that is not yet substantially equivalent may be individually exempt from the 150-hour education requirement and may be allowed to use practice privileges in this state if the individual was licensed prior to January 1, 2012.

(b) **A licensee of this state offering or rendering services or using their CPA title in another state shall be subject to disciplinary action in this state for an act committed in another state for which the licensee would be subject to discipline for an act committed in the other state. Notwithstanding Section 11(a), the Board shall be required to investigate any complaint made by the board of accountancy of another state.**

COMMENT: This section ensures that the Board of the state of the licensee's principal place of business, which has power to revoke a license, will have the authority to discipline its licensees if they violate the law when performing services in other states and to ensure that the state board of accountancy will be required to give consideration to complaints made by the boards of accountancy of other jurisdictions.

State of California Department of Consumer Affairs

CALIFORNIA BOARD OF ACCOUNTANCY
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Attachment 3

September 20, 2005

AICPA – UAA Committee
Allen G. Katz, CPA, Chair
1455 Pennsylvania Avenue, NW
Washington, DC 20004-1081

NASBA – UAA Committee
Samuel K. Cottrell, CPA, Chair
645 Fifth Avenue, Suite 901
New York, NY 10022

Dear Chairmen Katz and Cottrell:

The California Board of Accountancy (Board) appreciates the opportunity to comment on the August 1, 2005, UAA exposure draft. The Board applauds the efforts of the AICPA and NASBA UAA Committees toward improving and refining the UAA. We have limited our comments to those proposed changes that we believe merit further consideration by the UAA committees.

Proposed Definition of "Principal Place of Business"

As we understand it, the term "principal place of business" currently is not defined in the UAA. The exposure draft sets forth the following proposed definition: "'Principal place of business' means the office location designated by the licensee for purposes of substantial equivalency and reciprocity."

We have two concerns about the proposed definition. First, it is unclear to us why the term, which has an accepted meaning and usage throughout the country, requires definition in the UAA. Many states, including California, repeatedly use "principal place of business" in their accountancy acts, other statutes, and related regulations without defining that term. This lack of definition has not, as far as we are aware, created any problems of interpretation or impeded enforcement efforts. If there are reasons that came to the UAA committees' attention for providing a definition, we think it important to communicate them and to explain how the proposed definition addresses them.

Second, we are troubled by the proposed definition itself. As drafted, the definition would allow a licensee to designate virtually any office location as his or her "principal place of business." For example, a CPA licensed in multiple jurisdictions could, under the proposal, designate a principal place of business for substantial equivalency purposes that bears no relation to the licensee's *actual* principal place of business. Moreover, read literally, the proposed definition appears to foreclose a state board of accountancy from successfully challenging the licensee's designation: under the proposal, the principal place of business is whatever the licensee says it is. Finally, we are concerned that the proposed definition could result in the unintended consequence of subverting one of the primary prerequisites of the practice privilege: that the CPA's principal place of business *not* be in the visited state. We urge that the "principal place of business" be determined – as it is today – based on the facts and circumstances of each licensee's practice.

Peer Review

This Board supports the NASBA UAA Committee's proposal toward increasing transparency in the peer review process. We believe that transparency to the state boards is critical. Equally important, in our view, is transparency of certain peer review documents to the public. Accordingly, this Board cannot support any proposed revision to the UAA that precludes – as we believe the exposure draft does – a state board from adopting rules that allow for public access to certain peer review materials pertaining to licensees of that state. We urge the UAA committees to evaluate the possibility of exceptions to the confidentiality provisions of Section 7(h)(5) of the exposure draft.

Firm Practice Privilege

While developing the practice privilege process for California, this Board thoroughly explored the possibility of a notification process for firms. Ultimately, it decided not to pursue such a process for two reasons: first, in the context of notification, it was unclear that firms could accurately represent that each employee encompassed by the firm's blanket notification individually satisfied the requirements of Section 23; second, there appeared to be multiple significant enforcement issues raised by a process in which a firm – not the individuals – made representations and consented to conditions that purportedly bound the individuals.

We have the same concerns about the proposed Firm Permits to Practice. In addition, we believe that any process for firm notification should at a minimum obligate the firm to *establish* -- if called upon by a board and to its satisfaction – that each individual practicing under the firm's permit (Section 7(i)) or master notice (Section 7(j)) satisfies the state's substantial equivalency requirements. In our view, proposed Sections 7(i)(1)(A) and 7(j)(2) are insufficient insofar as they only impose on firms modest record-keeping requirements instead of the obligation to establish each individual's compliance with practice privilege standards.

Finally, we are unclear on the enforceability against an individual of a firm's consents and representations in the event that the individual leaves the firm. If the UAA committees have grappled with and solved these issues, we would benefit from an understanding of how the proposed process would not hamper enforcement efforts against a former employee of a firm.

We appreciate your consideration of our comments. If you have any questions, please feel free to contact the Board's Executive Officer, Carol Sigmann, at (916) 561-1718.

Sincerely,

Renata M. Sos
Board President

c: Members, California Board of Accountancy

State of California Department of Consumer Affairs

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Board Agenda Item II.B.1
February 23, 2006

5050. (a) Except as provided in subdivisions (b) and (c) of this section, subdivision (a) of Section 5054, and Section 5096.12, ~~No~~ no person shall engage in the practice of public accountancy in this state unless the person is the holder of a valid permit to practice public accountancy issued by the board or a holder of a practice privilege pursuant to Article 5.1 (commencing with Section 5096).

(b) Nothing in this chapter shall prohibit a certified public accountant, a public accountant, or public accounting firm lawfully practicing in another state from temporarily practicing in this state incident to practice in another state provided that the individual or firm does not solicit California clients and does not assert or imply that the individual or firm is licensed or registered to practice public accountancy in California. This subdivision shall become inoperative on January 1, 2010, and as of that date is repealed.

~~(b)~~ (c) Nothing in this chapter shall prohibit a person who holds a valid and current license, registration, certificate, permit or other authority to practice public accountancy from a foreign country, and lawfully practicing therein, from temporarily engaging in the practice of public accountancy in this state incident to an engagement in that country provided that:

(1) The temporary practice is regulated by the foreign country and is performed under accounting or auditing standards of that country.

(2) The person does not hold himself or herself out as being the holder of a valid California permit to practice public accountancy or the holder of a practice privilege pursuant to Article 5.1 (commencing with Section 5096).[1]

5050.1 Any person who engages in any act which is the practice of public accountancy in this state consents to the personal, subject matter, and disciplinary jurisdiction of the Board; and is deemed to have appointed the regulatory agency of the state or foreign jurisdiction that issued the person's permit, certificate, license or other authorization to practice as the person's agent on whom notice, subpoenas, or other process may be served in any action or proceeding by or before the Board against or involving that person.

[1] The language in subdivision (c) (in italics) was previously approved by the Board, recommended to the Legislature, and currently contained in SB 503.

5054. (a) Notwithstanding any other provision of this chapter, an individual or firm holding a valid and current license, certificate, or permit to practice public accountancy from another state may provide tax services ~~prepare tax returns for natural persons who are California residents or estate tax returns for the estates of natural persons who were clients at the time of death~~ without obtaining a permit to practice public accountancy issued by the board under this chapter or a practice privilege pursuant to Article 5.1 (commencing with Section 5096) provided that the individual or firm does not physically enter California to practice public accountancy pursuant to Section 5051, does not solicit California clients, and does not assert or imply that the individual or firm is licensed or registered to practice public accountancy in California.

(b) The board may, by regulation, limit the number of tax returns that may be prepared pursuant to subdivision (a).

(c) This section shall become inoperative on January 1, 2010, and as of that date is repealed.

[NOTE: Previous language to be restored after sunset date.]

5054.1 The Board may revoke, suspend or otherwise restrict or discipline the authorization to practice under subdivisions (b) or (c) of Section 5050, or subdivision (a) of Section 5054, or Section 5096.12 for any act which would be a violation of this chapter or ground for discipline against a licensee or practice privilege holder, or ground for denial of a license or practice privilege under the Code. The provisions of the Administrative Procedure Act, including, but not limited to, the commencement of a disciplinary proceeding by the filing of an accusation by the board shall apply to this Section. Any person whose authorization to practice under subdivisions (b) or (c) of Section 5050, or subdivision (a) of Section 5054, or Section 5096.12 has been revoked may apply for reinstatement of the authorization to practice under subdivisions (b) or (c) of Section 5050, or subdivision (a) of Section 5054, or Section 5096.12 not less than one year after the effective date of the board's decision revoking the temporary practice authorization unless a longer time, not to exceed three years, is specified in the board's decision revoking the temporary practice authorization.

5096.12 (a) A CPA firm that is authorized to practice in another state and which does not have an office in this state may engage in the practice of public accountancy in this state through the holder of a practice privilege provided that:

(1) The practice of public accountancy by the firm is limited to authorized practice by the holder of the practice privilege;

(2) The firm consents to the personal, subject matter, and disciplinary jurisdiction of the board with respect to any practice under this section;

(b) The board may revoke, suspend, or otherwise restrict or discipline the firm for any act which would be grounds for discipline against a holder of a practice privilege through which the firm practices.

5054. (a) Notwithstanding any other provision of this chapter, an individual or firm holding a valid and current license, certificate, or permit to practice public accountancy from another state may provide tax services ~~prepare tax returns for natural persons who are California residents or estate tax returns for the estates of natural persons who were clients at the time of death~~ without obtaining a permit to practice public accountancy issued by the board under this chapter or a practice privilege pursuant to Article 5.1 (commencing with Section 5096) subject to the restrictions ~~provided~~ that the individual or firm does not physically enter California to practice public accountancy pursuant to Section 5051, does not solicit California clients, and does not assert or imply that the individual or firm is licensed or registered to practice public accountancy in California.

(b) Not withstanding subdivision (a), any firm which is licensed to practice public accountancy in this state may provide the services set forth in subdivision (a) through individuals qualified to practice under subsection (a) however the restrictions of subsection (a) shall not apply to the firm.

~~(b)~~ (c) The board may, by regulation, limit the number of tax returns that may be prepared pursuant to subdivision (a).

(d) This section shall become inoperative on January 1, 2010, and as of that date is repealed.

[NOTE: Previous language to be restored after sunset date.]

State of California
Department of Consumer Affairs

California Board of Accountancy
2000 Evergreen Street, Suite 250
Sacramento, CA 95815-3832

Memorandum

CPC Agenda Item II.B
February 22, 2006

Board Agenda Item II.B.2.a
February 23, 2006

To : CPC Members
Board Members

Date: February 15, 2006

Telephone : (916) 561-1788
Facsimile : (916) 263-3674
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From : Aronna Wong
Legislation/Regulations Coordinator

Subject : Report on Pending Legislation: SB 503, Figueroa

Attached is SB 503 by Senator Figueroa as amended February 14, 2006 (Attachment 1). This bill contains statutory amendments sponsored by the Board. Specifically, SB 503 includes amendments to Business and Professions Code Section 5050 related to foreign accountants, amendments to Business and Professions Code Section 5134 related to fees, and amendments to Business and Professions Code Section 5076 related to peer review. It is anticipated that an urgency clause will be added to the bill when it is heard by the Assembly Business and Professions Committee.

The amendments to Sections 5050 and 5134 were approved by the Board at its meeting of January 20, 2006. As background information, Attachments 2 and 3 provide legislative proposals for these statutory amendments.

The amendments to Section 5076 related to peer review were included in the Board's August 24, 2005, Peer Review Report which was submitted to the Legislature. Attachment 4 provides excerpts from that report.

Attachments

AMENDED IN ASSEMBLY FEBRUARY 14, 2006

AMENDED IN ASSEMBLY JUNE 22, 2005

AMENDED IN SENATE APRIL 18, 2005

SENATE BILL No. 503

Introduced by Senator Figueroa

February 18, 2005

~~An act to amend Sections 6253.4 and 6253.9 of the Government Code, relating to public records.~~ *An act to amend Sections 5050, 5076, and 5134 of the Business and Professions Code, relating to accountants, and making an appropriation therefor.*

LEGISLATIVE COUNSEL'S DIGEST

SB 503, as amended, Figueroa. ~~Public records.~~ *Accountants.*

Existing law provides for the licensure and regulation of accountants by the California Board of Accountancy, in the Department of Consumer Affairs. Existing law prohibits a person from engaging in the practice of public accountancy unless the person holds a valid permit or a practice privilege, as specified. Existing law also requires a firm, other than a sole proprietor or a small firm, to meet specified peer review requirements prior to the first registration expiration date after January 1, 2008, in order to provide attest services. Existing law requires the board to review whether to implement the peer review program in light of changes in federal and state law or regulations or professional standards, and to report its findings to the Legislature by September 1, 2005. Existing laws sets specified fees to be charged by the board.

This bill would provide that a person with a valid and current license, registration, certificate, permit, or other authority to practice

public accountancy from a foreign country may temporarily engage in the practice of public accountancy in this state incident to an engagement in that country, if specified requirements are satisfied. The bill would require a firm to meet the peer review requirements within 3 years of the commencement of the peer review program, rather than prior to the first registration expiration date after January 1, 2008. The bill would revise the board's review and reporting requirement to instead require the board to review and evaluate whether to implement the program and report its findings and recommendations to the Legislature and the department no later than September 1, 2009. The bill would require that, if the board determines that the peer review program should be implemented, if identify the resources necessary for implementation and recommend a date for commencement. The bill would revise the fees to be charged by the board.

Because this bill may increase fees deposited into the Accountancy Fund, a continuously appropriated fund, it would make an appropriation.

~~(1) The California Public Records Act requires public records to be open to inspection at all times during the office hours of the state or local agency. Existing law authorizes every agency to adopt regulations stating the procedures to be followed when making its records available. Existing law requires specified state and local bodies to establish written guidelines for accessibility of records.~~

~~This bill would require each state or local body identified in existing law that maintains an Internet Web site, to make the written guidelines accessible from the homepage of its Web site through a link titled "Guidelines for How to Obtain Public Records."~~

~~(2) Existing law also requires, unless otherwise prohibited by law, any agency that has information that constitutes an identifiable public record not exempt from disclosure under the act that is in an electronic format to make that information available in an electronic format when requested by any person.~~

~~This bill would require an agency that maintains an Internet Web site and that has information that is an identifiable public record available to it in electronic format to make that information accessible to the public for a minimum of 3 years from the homepage of the agency's Web site through a link.~~

~~By imposing additional duties on local public agencies with regard to making public records accessible through a link to the local~~

~~agency's webpage, this bill would impose a state-mandated local program.~~

~~The California Constitution requires the state to reimburse local agencies and school districts for certain costs mandated by the state. Statutory provisions establish procedures for making that reimbursement.~~

~~This bill would provide that, if the Commission on State Mandates determines that the bill contains costs mandated by the state, reimbursement for those costs shall be made pursuant to these statutory provisions.~~

Vote: majority. Appropriation: ~~no~~ *yes*. Fiscal committee: yes. State-mandated local program: ~~yes~~ *no*.

The people of the State of California do enact as follows:

SECTION 1. Section 5050 of the Business and Professions Code is amended to read:

5050. (a) No person shall engage in the practice of public accountancy in this state unless the person is the holder of a valid permit to practice public accountancy issued by the board or a holder of a practice privilege pursuant to Article 5.1 (commencing with Section 5096).

(b) ~~This section shall become operative on January 1, 2006.~~ *Nothing in this chapter shall prohibit a person who holds a valid and current license, registration, certificate, permit or other authority to practice public accountancy from a foreign country, and lawfully practicing therein, from temporarily engaging in the practice of public accountancy in this state incident to an engagement in that country provided that:*

(1) The temporary practice is regulated by the foreign country and is performed under accounting or auditing standards of that country.

(2) The person does not hold himself or herself out as being the holder of a valid California permit to practice public accountancy or the holder of a practice privilege pursuant to Article 5.1 (commencing with Section 5096).

SEC. 2. Section 5076 of the Business and Professions Code is amended to read:

5076. (a) In order to renew its registration, a firm providing attest services, other than a sole proprietor or a small firm as

defined in Section 5000, shall complete a peer review ~~prior to the first registration expiration date after July 1, 2008,~~ *within three years of the commencement of the peer review program* and no less frequently than every three years thereafter.

(b) For purposes of this article, the following definitions apply:

(1) "Peer review" means a study, appraisal, or review conducted in accordance with professional standards of the professional work of a licensee or registered firm by another licensee unaffiliated with the licensee or registered firm being reviewed. The peer review shall include, but not be limited to, a review of at least one attest engagement representing the highest level of service performed by the firm and may include an evaluation of other factors in accordance with requirements specified by the board in regulations.

(2) "Attest services" include an audit, a review of financial statements, or an examination of prospective financial information, provided, however, "attest services" shall not include the issuance of compiled financial statements.

(c) The board shall adopt regulations as necessary to implement, interpret, and make specific the peer review requirements in this section, including, but not limited to, regulations specifying the requirements for the approval of peer review providers, and regulations establishing a peer review oversight committee.

(d) The board shall review *and evaluate* whether to implement the program specified in this section ~~in light of the changes in federal and state law or regulations or professional standards,~~ and shall report its findings *and recommendations* to the Legislature and the department ~~by~~ *no later than* September 1, ~~2005~~ *2009, as part of the review required by Division 1.2 (commencing with Section 473). If the board determines that the program specified in this section should be implemented, the board shall identify the resources necessary for implementation and recommend a date when the program shall commence.*

SEC. 3. Section 5134 of the Business and Professions Code is amended to read:

5134. The amount of fees prescribed by this chapter is as follows:

(a) The fee to be charged to each applicant for the certified public accountant examination shall be fixed by the board at an amount ~~to equal the actual cost to the board of the purchase or development of the examination, plus the estimated cost to the board of administering the examination and shall~~ not *to* exceed six hundred dollars ($600). The board may charge a reexamination fee ~~equal to the actual cost to the board of the purchase or development of the examination or any of its component parts, plus the estimated cost to the board of administering the examination and~~ not to exceed seventy-five dollars ($75) for each part that is subject to reexamination.

(b) The fee to be charged to out-of-state candidates for the certified public accountant examination shall be fixed by the board at an amount ~~equal to the estimated cost to the board of administering the examination and shall~~ not *to* exceed six hundred dollars ($600) per candidate.

(c) The application fee to be charged to each applicant for issuance of a certified public accountant certificate shall be fixed by the board at an amount ~~equal to the estimated administrative cost to the board of processing and issuing the certificate and shall~~ not *to* exceed two hundred fifty dollars ($250).

(d) The application fee to be charged to each applicant for issuance of a certified public accountant certificate by waiver of examination shall be fixed by the board at an amount ~~equal to the estimated administrative cost to the board of processing and issuing the certificate and shall~~ not *to* exceed two hundred fifty dollars ($250).

(e) The fee to be charged to each applicant for registration as a partnership or professional corporation shall be fixed by the board at an amount ~~equal to the estimated administrative cost to the board of processing and issuing the registration and shall~~ not *to* exceed two hundred fifty dollars ($250).

(f) The board shall fix the biennial renewal fee so that, together with the estimated amount from revenue other than that generated by subdivisions (a) to (e), inclusive, the reserve balance in the board's contingent fund shall be equal to approximately nine months of annual authorized expenditures. Any increase in the renewal fee ~~made after July 1, 1990,~~ shall be ~~effective~~ *made by regulation* upon a determination by the board~~,~~ ~~by regulation adopted pursuant to subdivision (k),~~ that additional

moneys are required to fund authorized expenditures ~~other than those specified in subdivisions (a) to (c), inclusive,~~ and maintain the board's contingent fund reserve balance equal to nine months of estimated annual authorized expenditures in the fiscal year in which the expenditures will occur. The biennial fee for the renewal of each of the permits to engage in the practice of public accountancy specified in Section 5070 shall not exceed two hundred fifty dollars ($250).

(g) The delinquency fee shall be 50 percent of the accrued renewal fee.

(h) The initial permit fee is an amount equal to the renewal fee in effect on the last regular renewal date before the date on which the permit is issued, except that, if the permit is issued one year or less before it will expire, then the initial permit fee is an amount equal to 50 percent of the renewal fee in effect on the last regular renewal date before the date on which the permit is issued. The board may, by regulation, provide for the waiver or refund of the initial permit fee where the permit is issued less than 45 days before the date on which it will expire.

(i) On and after January 1, 2006, the annual fee to be charged an individual for a practice privilege pursuant to Section 5096 shall be fixed by the board at an amount not to exceed ~~50 percent of the biennial renewal fee provided in subdivision (f)~~ *one hundred twenty-five dollars ($125)*.

(j) The fee to be charged for the certification of documents evidencing passage of the certified public accountant examination, the certification of documents evidencing the grades received on the certified public accountant examination, or the certification of documents evidencing licensure shall be twenty-five dollars ($25).

~~(k) The actual and estimated costs referred to in this section shall be calculated every two years using a survey of all costs attributable to the applicable subdivision.~~

~~(l)~~

(k) Upon the effective date of this section the board shall fix the fees in accordance with the limits of this section and, on and after July 1, 1990, any increase in any fee fixed by the board shall be pursuant to regulation duly adopted by the board in accordance with the limits of this section.

~~(m) Fees collected pursuant to subdivisions (a) to (e), inclusive, shall be fixed by the board in amounts necessary to recover the actual costs of providing the service for which the fee is assessed, as projected for the fiscal year commencing on the date the fees become effective.~~

(l) It is the intent of the Legislature that, to ease entry into the public accounting profession in California, any administrative cost to the board related to the certified public accountant examination or issuance of the certified public accountant certificate that exceeds the maximum fees authorized by this section shall be covered by the fees charged for the biennial renewal of the permit to practice.

All matter omitted in this version of the bill appears in the bill as amended in Assembly, June 22, 2005 (JR11)

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Attachment 2

PROPOSED LEGISLATION

Amend Business and Professions Code Section 5050:

The law changes that established the Practice Privilege Program (SB 1543, Figueroa, Chapter 921, Statutes of 2004) became effective on January 1, 2006, and included the repeal of the provision in Business and Professions Code Section 5050 which previously had permitted an accountant from another state or a foreign country to practice temporarily in California on professional business incident to his or her regular practice in such state or country.

The new Practice Privilege Program provides a mechanism for CPAs from other states in the United States to practice legally in California and clarifies the Board's regulatory oversight of these practitioners. However, after the repeal of this provision in Section 5050, neither the practice privilege provisions nor other provisions in current law permit accountants from foreign countries to lawfully practice in California.

At its January 19-20, 2006, meeting, the Board heard testimony from the profession that the absence of such a provision is a serious concern. It was noted that, for California to maintain its position in the global economy, foreign accountants must be able to come here temporarily to provide auditing and related services on behalf of foreign-based companies with subsidiaries or business interests in this state. These audit reports and other work products must be prepared under the professional standards and in compliance with the regulatory requirements of the foreign country, making it impractical for California CPAs to attempt to provide these vital services. Also, the Board has been informed that because of the regulatory deadlines in some foreign countries and the complexity of coordinating international work schedules, a legislative solution to address this issue is an urgent matter.

This proposal would add a new subdivision (b) to Business and Professions Code Section 5050 to address this concern. This language avoids the weaknesses of the repealed temporary practice provision which often left the determination of what constitutes temporary and incidental practice to the subjective judgment of each practitioner. This proposal, instead, confines the permitted temporary and incidental practice to work related to engagements in the foreign country, regulated by the foreign country, and performed under the accounting or auditing standards of that country. In this way the California activities that foreign accountants may undertake are distinguishable from and more limited than the activities permitted under the Practice Privilege Program available to out-of-state CPAs. Accordingly, California consumers are not placed at risk under this proposal.

There is no known opposition to this proposal, and it is anticipated that it will go forward as urgency legislation.

Proposed Amendment to Business and Professions Code Section 5050:

(a) No person shall engage in the practice of public accountancy in this state unless the person is the holder of a valid permit to practice public accountancy issued by the board or a holder of a practice privilege pursuant to Article 5.1 (commencing with Section 5096).

~~(b) This section shall become operative on January 1, 2006.~~

(b) Nothing contained in this chapter shall prohibit a person who holds an authorization to practice public accountancy from a foreign country, lawfully practicing therein, from temporarily practicing in this State incident to an engagement in that country provided that :

(1) The practice is primarily regulated by the accountant's country of licensure and is performed under accounting or auditing standards of that country; and

(2) The accountant does not hold himself or herself out as being licensed as a Certified Public Accountant or Public Accountant by the State of California.

State of California Department of Consumer Affairs

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Attachment 3

PROPOSED LEGISLATION

Amend Business and Professions Code Section 5134:

In September 2005 the California Board of again assessed its compliance with the requirements of its fee statute – Business and Professions Code Section 5134. Two areas of noncompliance were identified:

- Section 5134 requires that fees for license issuance be set at a level necessary to recover the cost of providing the service. However, the Board's cost of providing the service has for several years exceeded the revenue received from license issuance fees, even with the fee set at the maximum amount permitted by the statute. The cost of this service has been supported, in part, by revenue received from biennial renewal fees.
- Section 5134 mandates that the reserve balance in the Board's contingent fund be equal to approximately nine months of annual authorized expenditures. However, the reserve exceeds that amount and has been approximately equal to 14 months of authorized expenditures during the current fiscal year.

To address these areas of noncompliance the Board, after extensive dialogue with representatives of the profession, is proposing modifications to both the statute and to its implementing regulations.

For license issuance, a fee increase was considered and rejected by the Board because of a growing concern that increased costs would discourage qualified candidates from beginning careers in public accounting. Instead, this proposal would eliminate the statutory requirement that revenue generated by examination and license issuance fees be sufficient to support the Board's cost of providing these services. This proposal would add legislative intent language clarifying that, to ease entry into the profession, costs exceeding the maximum fees permitted for examination and license issuance would be covered by revenue from biennial renewal fees paid by licensed CPAs. Representatives of the profession have communicated no objection to this approach which would allow practicing CPAs, through their renewal fees, to lend a helping hand to new graduates and others seeking to enter the profession.

To address the matter of the reserve balance, the Board is in the process of lowering its biennial renewal fee through the rulemaking process. This proposal facilitates that rule change by eliminating the statutory language tying the fee for practice privilege to the biennial renewal fee so that the renewal fee can be reduced without simultaneously lowering the fee for practice privilege. The Practice Privilege Program which became operative on January 1, 2006, has staffing approved by the Department of Finance based on fees at the current level. Because the program is so new, it would be premature to modify the fee at this time.

This proposal also makes minor revisions to Section 5134 for clarity and consistency. The Board believes this proposal provides a framework for a workable fee structure that can be responsive to the needs of all stakeholders. There is no known opposition to this proposal.

Proposed Amendment to Business and Professions Code Section 5134.

The amount of fees prescribed by this chapter is as follows:

(a) The fee to be charged to each applicant for the certified public accountant examination shall be fixed by the board at an amount ~~to equal the actual cost to the board of the purchase or development of the examination, plus the estimated cost to the board of administering the examination and shall~~ not to exceed six hundred dollars ($600). The board may charge a reexamination fee ~~equal to the actual cost to the board of the purchase or development of the examination or any of its component parts, plus the estimated cost to the board of administering the examination and~~ not to exceed seventy-five dollars ($75) for each part that is subject to reexamination.

(b) The fee to be charged to out-of-state candidates for the certified public accountant examination shall be fixed by the board at an amount ~~equal to the estimated cost to the board of administering the examination and shall~~ not to exceed six hundred dollars ($600) per candidate.

(c) The application fee to be charged to each applicant for issuance of a certified public accountant certificate shall be fixed by the board at an amount ~~equal to the estimated administrative cost to the board of processing and issuing the certificate and shall~~ not to exceed two hundred fifty dollars ($250).

(d) The application fee to be charged to each applicant for issuance of a certified public accountant certificate by waiver of examination shall be fixed by the board at an amount ~~equal to the estimated administrative cost to the board of processing and issuing the certificate and shall~~ not to exceed two hundred fifty dollars ($250).

(e) The fee to be charged to each applicant for registration as a partnership or professional corporation shall be fixed by the board at an amount ~~equal to the estimated administrative cost to the board of processing and issuing the registration and shall~~ not to exceed two hundred fifty dollars ($250).

(f) The board shall fix the biennial renewal fee so that, together with the estimated amount from revenue other than that generated by subdivisions (a) to (e), inclusive, the reserve balance in the board's contingent fund shall be equal to approximately nine months of annual authorized expenditures. Any increase in the renewal fee ~~made after July 1, 1990,~~ shall be by regulation ~~effective~~ upon a determination by the board~~, by regulation adopted pursuant to subdivision (k),~~ that additional moneys are required to fund authorized expenditures ~~other than those specified in subdivisions (a) to (e), inclusive,~~ and maintain the board's contingent fund reserve balance equal to nine months of estimated annual authorized expenditures in the fiscal year in which the expenditures will occur. The biennial fee for the renewal of each of the permits to engage in the practice of public accountancy specified in Section 5070 shall not exceed two hundred fifty dollars ($250).

(g) The delinquency fee shall be 50 percent of the accrued renewal fee.

(h) The initial permit fee is an amount equal to the renewal fee in effect on the last regular renewal date before the date on which the permit is issued, except that, if the permit is issued one year or less before it will expire, then the initial permit fee is an amount equal to 50 percent of the renewal fee in effect on the last regular renewal date before the date on which the permit is issued. The board may, by regulation, provide for the waiver or refund of the initial permit fee where the permit is issued less than 45 days before the date on which it will expire.

(i) On and after January 1, 2006, the annual fee to be charged an individual for a practice privilege pursuant to Section 5096 shall be fixed by the board at an amount not to exceed ~~50 percent of the biennial renewal fee provided in subdivision (f)~~ one hundred and twenty-five dollars ($125).

(j) The fee to be charged for the certification of documents evidencing passage of the certified public accountant examination, the certification of documents evidencing the grades received on the certified public accountant examination, or the certification of documents evidencing licensure shall be twenty-five dollars ($25).

~~(k) The actual and estimated costs referred to in this section shall be calculated every two years using a survey of all costs attributable to the applicable subdivision.~~

~~(l)~~ (k) Upon the effective date of this section the board shall fix the fees in accordance with the limits of this section and, on and after July 1, 1990, any increase in any fee fixed by the board shall be pursuant to regulation duly adopted by the board in accordance with the limits of this section.

~~(m) Fees collected pursuant to subdivisions (a) to (e), inclusive, shall be fixed by the board in amounts necessary to recover the actual costs of providing the service for which the fee is assessed, as projected for the fiscal year commencing on the date the fees become effective.~~(l) It is the intent of the Legislature that, to ease entry into the public accounting profession in California, any administrative cost to the board related to the Certified Public Accountant examination or issuance of the Certified Public Accountant certificate that exceeds the maximum fees authorized by this section shall be covered by the fees charged for the biennial renewal of the permit to practice.

Attachment 4

PEER REVIEW REPORT

CALIFORNIA BOARD OF ACCOUNTANCY

Presented to the Joint Committee on Boards, Commissions and Consumer Protection of the California Legislature

Prepared in compliance with
Business and Professions Code Section 5076
Submitted August 24, 2005

RECOMMENDATIONS:

Based on the analysis and conclusions above, the Board respectfully makes the following recommendations:

1. Do not embrace the AICPA program at this time.

Because of the constraints and uncertainties discussed earlier in this report and in the 2003 Interim Report, it would not be prudent to embrace the AICPA Peer Review Program at this time. The Board has significant concerns about the AICPA program, particularly in two areas: transparency and scope.

2. Continue to evaluate options for the implementation of mandatory peer review in California and make a recommendation to the Legislature no later than the submission of the Board's September 2009 Sunset Review Report. Revise Business and Professions Code 5076 to indicate that the time frames for peer review implementation will be determined by the Legislature as part of the sunset review process.

At that time many of the above-noted uncertainties and constraints may have been resolved. Further, consideration of peer review as part of the sunset review process will permit the merits and drawbacks of peer review to be evaluated in the context of other Board programs – especially its underfunded and understaffed Enforcement Program – and the Legislature can give the Board guidance regarding resource allocation and priorities. **Attachment 13** provides statutory language to implement this recommendation. Any further discussions by the Board will be framed and defined by this report and the 2003 Interim Report.

3. The California Board of Accountancy must oversee mandatory peer review.

The details of the Board's oversight will be developed as part of any future consideration of mandatory peer review.

4. In any future study of mandatory peer review, consideration should be given to the transparency of peer review.

We believe that transparency both to the consumer and to state boards of accountancy is of critical importance. The nature, timing and availability of peer review documents to the public would be determined at a future time.

5. Exclude from any Board-mandated peer review program audits otherwise encompassed by the PCAOB inspection program.

Section 5076. Peer Review.

(a) In order to renew its registration, a firm providing attest services, other than a sole proprietor or a small firm as defined in Section 5000, shall complete a peer review ~~prior to the first registration expiration date after January 1, 2008,~~ within three years of the commencement of the peer review program and no less frequently than every three years thereafter.

(b) For purposes of this article, the following definitions apply:

(1)"Peer review" means a study, appraisal, or review conducted in accordance with professional standards of the professional work of a licensee or registered firm by another licensee unaffiliated with the licensee or registered firm being reviewed. The peer review shall include, but not be limited to, a review of at least one attest engagement representing the highest level of service performed by the firm and may include an evaluation of other factors in accordance with requirements specified by the board in regulations.

(2)"Attest services" include an audit, a review of financial statements, or an examination of prospective financial information, provided, however, "attest services" shall not include the issuance of compiled financial statements.

(c) The board shall adopt regulations as necessary to implement, interpret, and make specific the peer review requirements in this section, including, but not limited to, regulations specifying the requirements for the approval of peer review providers, and regulations establishing a peer review oversight committee.

(d) The board shall review and evaluate whether to implement the program specified in this section ~~in light of the changes in federal and state law or regulations or professional standards,~~ and shall report its findings and recommendations to the Legislature and the department ~~by~~ no later than September 1, ~~2005~~ 2009 as part of the review required by Division 1.2 of this code (commencing with Section 473). If the board determines the program specified in this section should be implemented, the board shall identify the resources necessary for implementation and recommend a date when the program shall commence.

Board Agenda Item II.B.2.a

defined in Section 5000, shall complete a peer review ~~prior to the first registration expiration date after July 1, 2008,~~ *within three years of the commencement of the peer review program* and no less frequently than every three years thereafter.

(b) For purposes of this article, the following definitions apply:

(1) "Peer review" means a study, appraisal, or review conducted in accordance with professional standards of the professional work of a licensee or registered firm by another licensee unaffiliated with the licensee or registered firm being reviewed. The peer review shall include, but not be limited to, a review of at least one attest engagement representing the highest level of service performed by the firm and may include an evaluation of other factors in accordance with requirements specified by the board in regulations.

(2) "Attest services" include an audit, a review of financial statements, or an examination of prospective financial information, provided, however, "attest services" shall not include the issuance of compiled financial statements.

(c) The board shall adopt regulations as necessary to implement, interpret, and make specific the peer review requirements in this section, including, but not limited to, regulations specifying the requirements for the approval of peer review providers, and regulations establishing a peer review oversight committee.

(d) The board shall review *and evaluate* whether to implement the program specified in this section ~~in light of the changes in federal and state law or regulations or professional standards,~~ and shall report its findings *and recommendations* to the Legislature and the department ~~by *no later than*~~ September 1, ~~2005 *2009, as part of the review required by Division 1.2 (commencing with Section 473)*~~. *If the board determines that the program specified in this section should be implemented, the board shall identify the resources necessary for implementation and recommend a date when the program shall commence.* 2010

SEC. 3. Section 5134 of the Business and Professions Code is amended to read:

5134. The amount of fees prescribed by this chapter is as follows:

State of California
Department of Consumer Affairs

California Board of Accountancy
2000 Evergreen Street, Suite 250
Sacramento, CA 95815-3832

Memorandum

CPC Agenda Item II.A
February 22, 2006

Board Agenda Item II.B.2.b
February 23, 2006

To : CPC Members
Board Members

Date: February 15, 2006
Telephone: (916) 561-1788
Facsimile : (916) 263-3674
E-mail: awong@cba.ca.gov

From : Aronna Wong - Aronna
Legislation/Regulations Coordinator

Subject : Report on Pending Legislation: AB 1868

Attached is AB 1868 by Assembly Member Bermudez as introduced January 17, 2006. This bill is sponsored by CalCPA to address problems that have occurred since the repeal, on January 1, 2006, of the temporary practice provision previously in Business and Professions Code Section 5050. These problems relate to practice by out-of-state firms and by accounting practitioners from foreign countries. The Board has been informed that amendments are planned, and the amended bill will be provided separately when it becomes available.

AB 1868, as introduced January 17, 2006, would make the following changes to existing law:

- AB 1868 would amend subdivision (a) of Business and Professions Code Section 5050 to delete the word "person" and replace it with "he or she." Subdivision (a) of Section 5050 is the prohibition against the unlicensed practice of public accountancy in California. While this amendment appears to be a matter of grammar, legal counsel has advised that this is a very substantive revision because as stated in Business and Professions Code Section 5035 "'Person' includes individual, partnership, firm, association, limited liability company, or corporation, unless otherwise provided." Legal counsel has indicated that by deleting the word "person" which includes both firms and individuals and replacing it with "he or she" which denotes individuals only, this amendment removes the requirement that a firm be registered and regulated by the Board. Consequently, under this law change, a variety of different entities including limited liability companies and general corporations would be allowed to engage in the unregulated practice of public accountancy in California.

- AB 1868 would also delete current subdivision (b) of Section 5050 which specifies a January 1, 2006, operative date. The bill would replace it with a new subdivision (b) which would permit temporary practice by a certified public accountant or a public accountant licensed in another state or country. This language is similar to the language that was in Section 5050 prior to January 1, 2006, except that the repealed provision used the more generic language "any accountant of a foreign country" rather than the more specific terms "certified public accountant" or "public accountant" which may not be the designations used by accounting professionals in foreign countries.

- In addition, AB 1868 would add a sunset date of January 1, 2009, for the amended version of Section 5050. The language currently in Section 5050 would be restored after the sunset date unless the provision is amended again prior to that date.

Attachment

ASSEMBLY BILL No. 1868

Introduced by Assembly Member Bermudez

January 17, 2006

An act to amend, repeal, and add Section 5050 of the Business and Professions Code, relating to accountancy.

LEGISLATIVE COUNSEL'S DIGEST

AB 1868, as introduced, Bermudez. Accountancy: licensure.

Existing law provides for the licensing and regulation of accountants by the California Board of Accountancy, in the Department of Consumer Affairs. Existing law requires a person engaging in the practice of public accountancy in this state to hold either a valid permit issued by the board or a practice privilege, as specified.

This bill would, until January 1, 2009, provide that this requirement does not apply to a certified public accountant or public accountant licensed and lawfully practicing in another state or a foreign country to the extent that he or she is temporarily practicing in this state incident to his or her regular practice.

Vote: majority. Appropriation: no. Fiscal committee: yes. State-mandated local program: no.

The people of the State of California do enact as follows:

SECTION 1. Section 5050 of the Business and Professions Code is amended to read:

5050. (a) No person shall engage in the practice of public accountancy in this state unless ~~the person~~ *he or she* is the holder of a valid permit to practice public accountancy issued by the

board or ~~a~~ *is the* holder of a practice privilege pursuant to Article 5.1 (commencing with Section 5096). *Nothing in this chapter shall prohibit a certified public accountant or public accountant licensed in either another state or a foreign country, and lawfully practicing therein, from temporarily practicing in this state incident to his or her regular practice in the state or country in which he or she is licensed.*

(b) ~~This section shall become operative on January 1, 2006.~~ *This section shall remain in effect only until January 1, 2009, and as of that date is repealed, unless a later enacted statute, that is enacted before January 1, 2009, deletes or extends that date.*

SEC. 2. Section 5050 is added to the Business and Professions Code, to read:

5050. (a) No person shall engage in the practice of public accountancy in this State unless he or she is the holder of a valid permit to practice public accountancy issued by the board or is the holder of a practice privilege pursuant to Article 5.1 (commencing with Section 5096).

(b) This section shall become operative on January 1, 2009.

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State of California
Department of Consumer Affairs

California Board of Accountancy
2000 Evergreen Street, Suite 250
Sacramento, CA 95815-3832

Memorandum

CPC Agenda Item II.A
February 22, 2006

Board Agenda Item II.B.2.b
February 23, 2006

To : CPC Members
Board Members

Date: February 21, 2006
Telephone: (916) 561-1788
Facsimile : (916) 263-3674
E-mail: awong@cba.ca.gov

From : Aronna Wong
Legislation/Regulations Coordinator

Subject : Report on Pending Legislation: AB 1868 – Amendments

Attached are amendments to AB 1868 by Assembly Member Bermudez which is being amended today. It is anticipated the amendments will be in print at the time of the Board meeting. AB 1868 as amended would make the following law changes:

- Amendments delete the temporary practice provision in the introduced version of the bill and add new language to permit temporary and incidental practice by a certified public accountant or public accountant licensed in another state or country who physically enters California to serve clients. It includes two restrictions: 1) that the practice be regulated by the accountant's state or country of licensure and 2) that the accountant not hold out as a California licensee or a California practice privilege holder. This appears to parallel the foreign accountant language sponsored by the Board, however there are the following differences: 1) the Board's language applies only to foreign accountants; 2) the Board's language requires the foreign accountant's work to be performed under the accounting or auditing standards of that accountant's country; 3) the Board's language uses generic terms to refer to the accountant from a foreign country rather than the terms "certified public accountant" or "public accountant" which may not be the correct designation of an accounting professional in a foreign country; and 4) the Board-sponsored provision is not restricted to certified public accountants who physically enter California.

- AB 1868 would add a sunset date for Section 5050. The sunset date in the introduced version of the bill was January 1, 2009. The amended bill changes that date to January 1, 2013. The introduced version of the bill indicated that the language currently in Section 5050 would be restored after the sunset date. The amended version of the bill deletes that provision.

- AB 1868 would amend subdivision (a) of Section 5054 to expand the range of services permitted under this exception. The current version of Section 5054 permits an exception from licensure and firm registration requirements for out-of-state CPAs and public accounting firms providing limited tax services and complying with certain restrictions. This exception is limited to preparing tax returns for natural persons or estate tax returns for the estates of natural persons who were clients at the time of death. AB 1868 would expand the permitted services to include all tax services, litigation support services, expert witness testimony, and consulting. Attest services would not be permitted. The restrictions in current law would remain, including the restriction against physically entering California, the restriction against soliciting California clients, and the restriction against asserting or implying that the individual or firm holds a California license or registration. The amendments would add a restriction against asserting or implying the individual holds a practice privilege and that California is not their principal place of business. AB 1868 also adds a sunset of January 1, 2013, for Section 5054.

Attachment

AMENDMENTS TO ASSEMBLY BILL NO. 1868

Amendment 1

In line 1 of the title, strike out ", repeal, and add Sections 5050" and insert:

and repeal Sections 5050 and 5054

Amendment 2

On page 2, line 2, strike out "Nothing in this chapter" and strike out lines 3 to 7, inclusive

Amendment 3

On page 2, line 8, after "(b)" insert:

Nothing in this chapter shall prohibit a certified public accountant or a public accountant licensed in another state or foreign country lawfully practicing therein from temporarily practicing in this state incident to an engagement in another state or country, provided that both:

(1) The temporary and incidental practice is regulated by the accountant's state or country of licensure.

(2) The accountant does not hold himself or herself out as being licensed or certified by this state or as the holder of a practice privilege pursuant to Article 5.1 (commencing with Section 5096).

This subdivision applies only to certified public accountants who physically enter California to provide services to clients.

(c)

Amendment 4

On page 2, line 9, strike out "2009" and insert:

2013

Amendment 5

On page 2, line 11, strike out "2009" and insert:

2013

Amendment 6

On page 2, strike out lines 13 to 20, inclusive, and insert:

SEC. 2. Section 5054 of the Business and Professions Code is amended to read:

5054. (a) Notwithstanding any other provision of this chapter, an individual or firm holding a valid and current license, certificate, or permit to practice public accountancy from another state may ~~prepare tax returns for natural persons who are California residents or estate tax returns for the estates of natural persons who were clients at the time of death~~ perform tax services, litigation support, expert witness testimony, or consulting incidental to their practice in another state without obtaining a permit to practice public accountancy issued by the board under this chapter or a practice privilege pursuant to Article 5.1 (commencing with Section 5096) provided that the individual or firm does not physically enter California to practice public accountancy pursuant to Section 5051, does not solicit California clients, and does not assert or imply that the individual or firm is licensed or registered to practice public accountancy in California or a holder of a practice privilege pursuant to Article 5.1 (commencing with Section 5096) and California is not their principal place of business.

(b) The board may, by regulation, limit the number of tax returns that may be prepared pursuant to subdivision (a).

(c) This section shall remain in effect only until January 1, 2013, and as of that date is repealed unless a later enacted statute, that is enacted before January 1, 2013, deletes or extends that date.

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